FINANCIAL REPORTING

MESSAGE FROM THE CHIEF FINANCIAL OFFICER

I am pleased to submit the U.S. Small Business Administration's (SBA) Performance and Accountability Report for FY 2003. This report provides the SBA's program and financial results as required by the Reports Consolidation Act.

FY 2003 was a year of substantial accomplishment for the SBA in the area of financial management. The Office of the Chief Financial Officer (OCFO) made tremendous improvements in its cost estimates for all of its major loan programs and achieved its objectives in the administrative accounting and budget arena as well. While we are disappointed that these achievements did not result in an improved independent audit opinion, we are proud of the progress we have made and are confident that our efforts have substantially improved the quality of our financial statements.

Last year, the SBA's independent auditor issued a "disclaimer" for our FY 2002 financial statements. The primary issues leading to the disclaimer were the budgeting and accounting for the Agency's loan asset sales program and the SBA's ability to estimate the residual asset or liability in the Master Reserve Fund (MRF) associated with the Secondary Market Guarantee program. Over the past year, the OCFO conducted extensive analyses of these problems, completed the work recommended by the independent auditor, and successfully resolved virtually all of the key issues.

Unfortunately, despite the work completed, the independent auditor was again this year unable to satisfy itself that the SBA's financial statements fairly represent the financial position of the Agency at year end FY 2002 and FY 2003. The primary reason for the disclaimed opinion this year was that SBA was late in completing its models and financial statements and did not leave sufficient time for the auditor to conduct its testing and reviews, particularly of the credit subsidy models and related accounting transactions. We accept responsibility for this result and agree that further improvements are necessary. The ambitious subsidy model development agenda we developed to address last year's audit findings ultimately required more time than was available, which left insufficient time for the SBA to complete its established quality assurance review process prior to the completion of the financial statements. Therefore, the draft financial statements delivered to the auditor did not have the benefit of our planned review process. We did complete a subsequent version of the financial statements which included most of the auditor's findings, but the auditor did not have sufficient time to complete its review of those materials. SBA believes the final statements contained in this report provide a fair representation of the Agency's financial condition including the restatement of FY 2002 results, but we recognize that our untimely process did not leave the auditor sufficient time to form its own opinion. Completing our financial reporting work in a timely and thorough manner is the highest financial management priority for SBA in FY 2004.

To address last year's audit finding, the OCFO developed a new budget model to estimate the cost of the Disaster loan program and the impact of the asset sales program. We found that the previous Disaster loan program model had been underestimating the baseline program cost. We also found that the Disaster "hold" model used for the loan sales was substantially underestimating the cost of the loans being sold. Because of this, the sale of Disaster loans was not profitable as the Agency had previously believed. Consequently, the asset sales program was discontinued this year. The SBA recorded a net upward reestimate of $978 million this year to reflect the resolution of these issues for FY 2001-2003. The losses on all of the loan asset sales totaled $828 million. The SBA's new loan-level Disaster credit subsidy model was designed to be used for both the loan sale valuations and the subsidy reestimates to ensure consistency across the budget and accounting computations. The large upward reestimates have substantially resolved the "unnatural balances" problem identified by the independent auditor and GAO last year. We are confident that the new Disaster model will be an effective tool in measuring the cost of the program going forward and that this problem has been resolved.

The OCFO also developed a new model to estimate the residual asset or liability of the MRF as recommended last year by the independent auditor. Rather than relying on a sample of loan pools as had been done in the past, the OCFO obtained data for all of the loans and pools in the Secondary Market Guarantee program and used that information to develop the new model. We also used the default and prepayment forecasts from the 7(a) Loan Guarantee model as an input to the model to ensure consistency across the models, since all loans in the Secondary Market Guarantee program are 7(a) loans. The model was reviewed and validated by Ernst & Young, LLP and SBA is confident that the results of the model forecast are a reasonable representation of the Agency's liability for this program. However, the independent auditor did not have sufficient time to complete its own review and therefore this issue is a component of the disclaimed opinion again this year.

The SBA undertook a number of other initiatives this year to address the FY 2002 independent auditor's recommendations including:

- Resolving the issue regarding the liability for loan guarantees and related accounts for pre-1992 loan commitments;
- Adding resources to and reengineering components of our financial reporting process, including hiring Ernst & Young, LLP to advise and support us on all aspects of our financial reporting and to review our credit models; and
- Developing several new reports and protocols for ensuring adequate funds control in the loan fund liquidating and financing accounts.

In addition to addressing the audit findings from last year, SBA also completed a new econometric model for the 504 loan program that will be used for the FY 2005 loan cohort and for reestimates beginning in FY 2004. In FY 2002, SBA completed a new 7(a) econometric model that was used for the FY 2003 7(a) loan cohort. This year, we added functionality to the model so that it could be used for the reestimates in the FY 2003 financial statements.

FY 2003 was the SBA's second year with its new administrative accounting system based on Oracle's Federal Financial software. During the year, SBA switched to a new provider to host the Oracle software. This change enabled the Agency to lower the cost of operating the system. Because of this cost savings, we will be able to complete a software upgrade in FY 2004 that will provide additional administrative accounting functionality.

The SBA also made important progress in budget and performance integration this year. We continued to use and improve upon our cost accounting model. The Agency completed a new five year strategic plan in September, so we are now well positioned to achieve consistency across our strategic plan and our budget and accounting formulation and execution reports. Our program and results cost estimates continue to improve and the SBA demonstrated its commitment to using this information in the budget allocation process this year.

In summary, FY 2003 was a very productive year in financial management at the SBA. While we recognize there are still many challenges, we are confident that the progress we have made will continue to bear fruit for us in the coming year as we approach the accelerated financial statement reporting deadline of November 15th for FY 2004. We will continue to use the principles of the President's Management Agenda as a guide for the SBA's initiatives to improve financial performance in the coming year. Thank you for your interest in our FY 2003 Performance and Accountability Report.

Thomas Dumaresq
Chief Financial Officer

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Independent Auditor's Report

Inspector General
U.S. Small Business Administration

We were engaged to audit the accompanying consolidated balance sheets of the U.S. Small Business Administration (SBA) as of September 30, 2003, and 2002; related consolidated statements of net cost, changes in net position, and financing; and combined statements of budgetary resources for the years then ended. These financial statements are the responsibility of SBA management.

The scope of our examination was limited, because SBA was late in completing development and testing of certain credit program subsidy models, completing its credit program subsidy re-estimates, and preparing its financial statements. As a result, adequate time did not remain to obtain sufficient, competent, evidential matter; apply auditing procedures necessary to conduct an audit in accordance with generally accepted auditing standards and generally accepted government auditing standards; and form a reasonable basis for an opinion on the financial statements by the January 30, 2004, reporting deadline specified by the Office of Management and Budget (OMB) Memorandum titled Fiscal Year (FY) 2003 Financial and Performance Reporting (August 13, 2003.)

Because we were unable to apply all necessary auditing procedures to conduct an audit in accordance with generally accepted auditing standards or dispose of reservations identified during our work, we are not able to express, and we do not express, an opinion on SBA's FY 2003 and 2002 financial statements.

Cotton & Company identified certain matters causing us reservations regarding whether particular financial statement amounts and disclosures are presented fairly in accordance with prevailing federal accounting standards. Because of the time delays discussed above, we were not able to apply all of the auditing procedures that may have allowed us to resolve our reservations before the due date specified in OMB's August 13, 2003, memorandum. These reservations are discussed below.

Secondary Market Guarantee Subsidy Cost and Liability

During FY 2003, SBA developed a model to forecast the residual liability or asset in the Master Reserve Fund maintained by SBA's fiscal and transfer agent to facilitate operation of the Section 7(a) secondary market guarantee program. As a result of both SBA's internal testing and independent verification and validation of the model, the original estimated liability was materially revised several times, indicating high control risk regarding this estimate. In addition, SBA did not have sufficient time to complete its model documentation or perform and document an analysis to ensure the completeness and accuracy of data used in the model, which is provided by its fiscal and transfer agent. Model documentation and the data analysis are required evidential audit matter to support the estimate. As a result, we were not able to satisfy ourselves regarding the estimate and related liability for the secondary market guarantee program.

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Credit Program Receivables in Guaranteed Loan Programs

SBA records an adjusting journal entry to realign its balances between the Liability for Loan Guarantees and the Allowance for Subsidy accounts to properly value its credit program receivables on defaulted guaranteed loans. We noted problems with the quality of the analysis used to determine the realignment entry. In response to our concerns, SBA revised its analysis and posted a revised realignment entry. Time limitations precluded us from reviewing SBA's revised analysis and accounting entry.

SBA did not record a required adjusting journal entry to realign its balances in the Liability for Loan Guarantees and Allowance for Subsidy accounts related to prioritized payments made to investors under the Small Business Investment Company (SBIC), Participating Securities program, before issuing its draft financial statements on December 22, 2003. At our request, SBA estimated the realignment amount and recorded an adjusting entry for its final financial statements; time limitations precluded us from reviewing it.

Restated Gain or Loss on Asset Sales

SBA conducted an analysis to calculate revised gain/loss on loans sold during FYs 1999 through 2003. SBA computed a revised net book value using various assumptions depending on the program and available data. The revised net book value was subtracted from the loan sale proceeds to calculate a revised gain/loss. We noted concerns with the data used in this analysis for the Section 7(a) and 504 guaranteed business loan programs and communicated our concerns to management. SBA did not respond to our concerns in time for us to complete our review of the revised gain/loss calculation. SBA disclosed a $163 million and $126 million change between previously reported losses and revised gains in its Section 7(a) and 504 credit programs.

Footnote Disclosures

SBA provided Cotton & Company with a draft of its financial statements on December 22, 2003; these statements and related footnote disclosures contained substantial errors, omissions, inconsistencies, and other inadequacies. Although SBA addressed some of our concerns, we continue to have reservations regarding footnote disclosures, particularly the disclosures related to subsidy re-estimates, asset sales, and adjustments to the restated FY 2002 financial statements. We did not have sufficient time to satisfy ourselves as to the accuracy, completeness, and adequacy of the disclosures.

We noted three additional matters causing us reservations regarding the fair presentation of SBA's financial statements.

Liabilities for Loan Guarantees and Credit Program Receivables and Related Foreclosed Property, Net

SBA made noteworthy strides toward accomplishing its objectives to develop new or enhance existing models to improve the reasonableness of its credit program estimates during FY 2003. SBA was not, however, able to complete an analysis to ensure that its financing fund account balances are fairly stated.

We noted that SBA's general ledger account balances comprising Liabilities for Loan Guarantees and Credit Program Receivables and Related Foreclosed Property, Net, were not in alignment with the present value of forecasted cash flows produced by the credit program subsidy models. Our preliminary analysis shows substantial differences in the Small Business Investment Company Participating Securities, Section 7(a) and 504 Business, and Disaster Loan programs. In addition, account balances for some cohorts are not plausible based on re-estimated subsidy rates and the nature of the programs.

Adjustment to Interest Expense on Borrowing, Net

SBA performed an analysis of its financing account balances for the Disaster Loan program and found an inconsistency between the interest rate(s) used to discount cash flow estimates (used for subsidy rates and re-estimates) and the interest rate(s) used to compute interest earnings on cash balances and interest expense on borrowings from Treasury. The equality of these rates is required specifically in the Federal Credit Reform Act, as amended, and is fundamental to achieving the proper balance in the financing fund. This stems from using different tools to discount cash-flow estimates and calculate interest transactions with Treasury; each tool computes the cohort weighted average rate(s) using different schemes.

SBA determined that interest expense paid to Treasury (net of interest earned on uninvested funds) since the inception of credit reform, has been consistently overstated; SBA estimated that the excess interest expense compounded to account for lost interest earnings on uninvested funds was $128.7 million. SBA treated this overstatement as a current-year re-estimate, which overstates the cost of the Disaster assistance program, rather than as a decrease in current and prior year interest expense transactions with Treasury. As a result, subsidy costs were overstated in FY 2003, and interest expense for FY 2003 and prior years was overstated.

SBIC Participating Securities Re-estimates

SBA made enhancements to its SBIC Participating Securities credit subsidy model, which uses both historical data and expert opinion to estimate program subsidy cost. SBA increased its default assumptions (on guaranteed securities) and decreased its recovery assumptions based on a portfolio analysis and an increase in actual defaults resulting in part from the substantial economic downturn experienced by the venture-capital industry over the past several years.

We have reservations, however, about the reasonableness of other assumptions in the model, particularly the forecast for reimbursement by SBICs of prioritized payments (interest payments made by SBA to investors) and SBA's profit participation in SBIC returns on investments. These forecasts do not appear reasonable based on program experience to date and the revised assumption for net defaults. Accordingly, the subsidy cost, credit program receivables, net, and liabilities for loan guarantees may be misstated.

*** *** ***

Information presented in SBA management's discussion and analysis, required supplementary stewardship information, required supplementary information, and other accompanying information are not required parts of the financial statements, but are additional information required by the Federal Accounting Standards Advisory Board and OMB Bulletin 01-09, *Form and Content of Federal Financial Statements.* This information has not been subjected to auditing procedures and, accordingly, we express no opinion on it.

In accordance with *Government Auditing Standards*, we have also issued reports dated January 28, 2004, on our consideration of SBA's internal control and on its compliance with laws and regulations. Those reports, which disclose material weaknesses and reportable conditions in internal control and non-compliance with certain laws and regulations and the Federal Financial Management Improvement Act, are integral parts of a report prepared in accordance with *Government Auditing Standards* and should be read in conjunction with this report in considering the results of our work.

COTTON & COMPANY LLP

Charles Hayward, CPA

January 28, 2004
Alexandria, Virginia

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Independent Auditor's Report on Internal Control

Inspector General
U.S. Small Business Administration

We were engaged to audit the financial statements of the U.S. Small Business Administration (SBA) as of and for the years ended September 30, 2003, and 2002, and have issued our report thereon, dated January 28, 2004, in which we disclaimed an opinion on those financial statements. Such financial statements are the responsibility of SBA management.

In planning and performing our work, we considered SBA's internal control over financial reporting by obtaining an understanding of SBA's internal control, determining if internal control had been placed in operation, assessing control risk, and performing tests of control. We limited internal control testing to those controls necessary to achieve objectives described in the Office of Management and Budget (OMB) Bulletin No. 01-02, *Audit Requirements for Federal Financial Statements.* We did not test all internal controls relevant to operating objectives as broadly defined by the Federal Managers' Financial Integrity Act of 1982 (FMFIA), such as those controls relevant to ensuring efficient operations. The objective of our work was not to provide assurance on internal control. Consequently, we do not provide an opinion on internal control.

Our consideration of internal control over financial reporting would not necessarily disclose all matters in internal control over financial reporting that might be reportable conditions. Under standards issued by the American Institute of Certified Public Accountants (AICPA) and OMB Bulletin No. 01-02, reportable conditions are matters coming to our attention relating to significant deficiencies in the design or operation of internal control that, in our judgment, could adversely affect SBA's ability to record, process, summarize, and report financial data consistent with management assertions in the financial statements.

Material weaknesses are reportable conditions in which the design or operation of one or more internal control components does not reduce to a relatively low level the risk that misstatements in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. Because of inherent limitations in internal control, misstatements, losses, or noncompliance may nevertheless occur and not be detected.

We noted three matters involving internal control and its operation that we consider to be reportable conditions. These matters are described below under the captions: Credit Reform Controls, Financial Management and Reporting Controls, and Agency-Wide Information Systems Controls. We consider the first two matters to be material weaknesses under standards established by AICPA and OMB Bulletin No. 01-02.

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1. CREDIT REFORM CONTROLS

SBA's credit reform environment lacks the following key controls:

- Standard operating procedures for the re-estimate process.
- Documentation supporting cash flow models.
- Procedures to ensure completeness and accuracy of historical accounting data used in the cash flow models.
- Control over valuation of the Fiscal Year (FY) 2003 Small Business Investment Company (SBIC) Participating Security (PS) program subsidy re-estimate.
- Procedures to ensure the accuracy of inputs and outputs for the Credit Subsidy Calculator and Consolidated Credit Tools.
- Procedures to identify and explain unusual subsidy balances.

STANDARD OPERATING PROCEDURES FOR THE RE-ESTIMATE PROCESS

The Office of Chief Financial Officer (OCFO) does not have documented standard operating procedures (SOPs) to address SBA's current subsidy re-estimate process. The internal control procedures within SBA's subsidy re-estimate preparation process are, for the most part, not documented—thus undermining their effectiveness by:

- Creating possible process and procedural inconsistencies among programs.
- Increasing the potential for inaccurate subsidy re-estimates due to incomplete/inadequate review.

SBA made noteworthy accomplishes in developing new or enhancing existing credit subsidy models during FY 2003 to improve the reasonableness of its credit program subsidy estimates. While SBA was able to develop, test, and implement significant model changes, it did not have sufficient time and resources to fully develop and document standard operating procedures for calculating re-estimates and establishing other internal controls.

The Federal Accounting Standards Advisory Board's (FASAB) Credit Reform Task Force (Accounting and Auditing Policy Committee), Technical Release No. 3, Preparing and Auditing Direct Loan and Loan Guarantee Subsidies under the Federal Credit Reform Act (Tech Release No. 3), states that agencies should:

> "Document the procedures and flow of information used in developing the agency's subsidy estimates at a high level, e.g., flow chart with supporting narrative. These documents should be used to establish consistent procedures for developing the subsidy estimates across funds/programs/cohorts. These documents should also include a discussion of who is responsible for each step of the estimate as well as the review and approval process followed."

Recommendation

1A. We recommend that the Chief Financial Officer (CFO) develop a comprehensive SOP detailing the subsidy re-estimate process, including related internal controls, that reflects SBA's current re-estimate preparation processes and any proposed improvements. The new SOP should be updated at least annually to capture significant changes such that it reflects the current operating process.

DOCUMENTATION SUPPORTING CASH FLOW MODELS

SBA's cash flow models for its following material credit programs were not adequately documented:

- Section 7(a) Business Loan Guarantee Program
- SBIC Program

Computer-based model documentation is a critical control to ensure that models are usable and understandable to both technical and non-technical users and that they are adequately maintained over time. In addition, model documentation serves as a required audit trail to facilitate internal and external verification and validation functions. Tech Release No. 3 provides that agencies should:

> "Document the agency's cash flow model(s) used, the rationale for selecting the specific methodologies, and the degree of calibration within the model(s). Also, document the sources of information, the logic flow, and the mechanics of the model(s) including the formulas and other mathematical functions. In addition, document the controls over the model(s) used by the agency in preparing cash flow worksheets. Further, document that the cash flow model(s) reflect the terms of the loan contracts and, in a loan guarantee program, the loan guarantee contracts."

Documentation deficiencies are detailed below by program.

Section 7(a) Business Loan Guarantee Program

OCFO contracted with an outside entity to develop its Section 7(a) econometric model, which was first used to develop the 2003 cohort execution subsidy rate and later used for the FY 2003 re-estimates. It is our understanding that the majority of the resources provided to the model developer were used to develop the model; although documentation was prepared it contained the following deficiencies:

- The model version and history are not stated.

- The statistical routine used was not clearly identified or discussed in the documentation.

- No technical references exist. Specifically, there is no reference for the statistical method (multinomial logit) used for the performance model or for the JAVA code used to populate input to the performance model and convert performance model output into cash flows.

- Several important variables are not clearly identified. Units of measure for some key variables are not specified.

- There is no mathematical specification of the models.

- The results of the default and prepayment model (computed default and prepayment conditional probabilities) are not shown or discussed, and the manner in which recovery and cash flow projection components use these results is neither shown clearly nor explained.

- There is no discussion of the assumptions and limitations of a multinomial logit approach.

- The documentation is self-contradictory about the quality of the default and prepayment model.

- The documentation on model performance contains graphs that are mislabeled; in addition, there is no discussion of what the observations shown by the graphs (which are questionable due to the mislabeling) signify in assessing model quality.

Aside from the above shortcomings, we could not determine if analyses generally performed in developing multinomial logit models were completed by SBA or its developer with respect to the Section 7(a) model, because documentation did not exist. For instance, a likelihood ratio test of the model with most variables omitted, or constrained to be zero, versus the selected model and comparisons of predicted versus actual default and prepayment probabilities for subgroups of the population are part of standard practice for this type of model as recommended in the statistics package utilized by the developer. Documentation of these analyses was not available.

SBIC Program

Except for documentation regarding the default and recovery expert opinion assumptions revised during FY 2003, documentation generally was not sufficient to support the SBIC cash flow models' data sources, logic flow, mechanics, and explicit assumptions developed historically by the Investment Division.

Recommendations

We recommend that the CFO:

1B. Complete the Section 7(a) model documentation in accordance with Tech Release No. 3 and assure that the shortcomings we identified are addressed by the documentation. In addition, perform and document the likelihood ratio test and comparison of predicted versus actual default and prepayment probabilities for subgroups of the population.

1C. Direct a coordinated effort among OCFO (the Office of Financial Analysis) and Investment Division to fully document the SBIC program models in accordance with Tech Release No. 3.

PROCEDURES TO ENSURE COMPLETENESS AND ACCURACY OF HISTORICAL ACCOUNTING DATA USED IN THE CASH FLOW MODELS

Historical loan-level transactional data (or "actuals") are an integral element of SBA's cash flow models. SBA's controls were, however, insufficient to ensure that such historical data were reliable and complete. We noted the following control deficiencies.

Loan Accounting System Actual Cash Flow Transactions Were Unreliable [Disaster Assistance and Section 7(a)]

The Disaster Assistance and Section 7(a) loan programs both use historical loan-level transactions extracted from SBA's Loan Accounting System (LAS) to populate "actuals" in the subsidy re-estimate model. SBA lacked effective internal control to ensure the completeness and accuracy of historical transactions used in the cash flow models. The following errors were noted:

- Section 7(a) Supplemental Terrorist Activity Relief (STAR) program accounting transactions were improperly included in the Section 7(a) program re-estimate for the 2002 and 2003 cohorts. The initial re-estimates, including STAR data, resulted in downward re-estimates of $93 million. The revised re-estimates without STAR data resulted in a net upward re-estimate of $14 million for a combined change of $107 million.

- OCFO did not include $8.4 million of actual defaults in the 2002 cohort Section 7(a) re-estimate as the result of a programming error.

- SBA did not include actual sale proceeds that had previously been reserved to cover potential claims for representations and warranties in its initial Disaster Assistance program re-estimate. During FY 2003, SBA determined that its reserve was no longer needed and recorded the cash transaction in the financing fund at a summary-versus-loan-level. This summary level cash inflow was not picked up in the cash flow model, because the model generally is only populated with loan-level detail. Persons responsible for calculating the re-estimate were not aware that this summary-level cash transaction had been recorded in the Financing fund. SBA recorded an adjustment to correct this $58 million error in its Disaster re-estimate.

Tech Release No. 3, states:

> "The budget and accounting offices should work together to ensure that cash flow models are updated to reflect the actual cash flows and terms of the loan program recorded in the accounting records."

Recommendations

We recommend that the CFO:

1D. Direct the Office of Financial Analysis to clearly define which programs (subprogram codes) should be included in the Section 7(a) re-estimate actuals.

1E. Direct the Office of Financial Analysis and applicable personnel in the Office of the Chief Information Officer to develop a quality assurance system to ensure that data extracted from LAS for inclusion in the subsidy re-estimate models are complete and accurate.

SBIC Program Data Used for Modeling Not Reconciled to Accounting System

SBA does not have effective internal control to ensure the completeness and accuracy of historical accounting transactions used in the SBIC credit subsidy models to calculate re-estimates. SBA's LAS does not contain the necessary level of detail to produce historical loan transactions for subsidy re-estimates for the SBIC program, because:

- Many transactions processed in LAS are not cohort specific (re-estimates must be calculated at the cohort level).

- The timing of cash flows is often not correct as the result of SBA's practice of recording SBIC cash transactions into clearing accounts until the proper accounting treatment can be identified.

Shortcomings in LAS transactional data prompted the Office of Financial Analysis personnel to use program data provided by the Investment Division for calculating subsidy re-estimates. Because data from Investment Division were not derived from LAS, they were not subject to OCFO's system and manual data controls. To ensure the reliability of Investment Division data, the Office of Financial Analysis attempted to reconcile SBIC PS program data per Investment Division records to LAS. Unexplained reconciling items remained in several cash flow categories. The Office of Financial Analysis did not perform a similar reconciliation for the SBIC debentures program.

We performed a reconciliation of Investment Division data for both SBIC programs with LAS data, and noted that data were consistent at the program level; they were, however, inconsistent at the cohort level or within activity year. These differences are most likely the result of processing issues noted above.

Tech Release No. 3, states:

> "The budget and accounting offices should work together to ensure that cash flow models are updated to reflect the actual cash flows and terms of the loan program recorded in the accounting records."
>
> "The accounting office should maintain detailed subsidiary accounting records by program, cohort, and case."

Although we were able to perform other procedures to draw conclusions about the reasonableness of Investment Division data, it is management's responsibility to develop a system of control to ensure that data used to produce estimates are complete and accurate. Without such a control, SBIC subsidy re-estimates could be questionable, and cash flow projections produced by the subsidy model could differ from the expected value of future cash flows in the accounting system.

Recommendations

We recommend that the CFO:

1F. Direct the Office of Financial Analysis to develop, as an interim measure, an internal control procedure to reconcile the Investment Division SBIC PS and Debenture transaction data to LAS at the cohort and activity-year level; research and fully explain all variances; and determine if Investment Division data are appropriate for use in subsidy re-estimates.

1G. Begin recording all SBIC transactions in the proper fiscal year and cohort and add SBIC-specific transaction codes to LAS, as necessary, to better identify SBIC activity, so that SBIC subsidy re-estimate actuals can be derived from LAS in the future.

Secondary Market Guarantee Data Not Validated

SBA could not provide sufficient evidential matter in a timely fashion to support either the completeness or the accuracy of data provided to SBA by its fiscal and transfer agent; these data were used in SBA's model to project the future cash flows of existing loans and investment pools and in turn the shortfall in the Master Reserve Fund maintained by the fiscal and transfer agent to facilitate operation of SBA's Secondary Market Guarantee program. While SBA provided a document titled *Secondary Market Guarantee Model Data Sources and Validations,* this document did not sufficiently describe or provide evidence of procedures performed to establish the completeness and accuracy of data used.

Statements of Federal Financial Accounting Standards (SFFAS) Number 2, *Accounting For Direct Loans and Loan Guarantees*, states:

> "The effort to make accurate projections should begin with establishing and using reliable records of historical credit performance data."

Recommendation

We recommend that the CFO:

1H. Develop, document, and implement data quality assurance procedures to establish the completeness and accuracy of data provided by SBA's fiscal and transfer agent for Secondary Market Guarantee estimation purposes.

CONTROL OVER VALUATION OF THE FY 2003 SBIC PARTICIPATING SECURITY PROGRAM SUBSIDY RE-ESTIMATE

SBA could not support the reasonableness of the FY 2003 SBIC PS program re-estimate ($1.8 billion upward re-estimate), because the basis for selecting and developing the forecast assumptions for reimbursement of prioritized payments and SBA profit participation in SBICs' returns on investments was not sufficiently reviewed and documented.

Tech Release No. 3 provides:

> "The cash flow estimation process, including all underlying assumptions, should be reviewed and approved at the appropriate level including revisions and updates to the original model. Cash flow models should be tested for reliability as part of the approval process by comparing estimated cash flows to actual cash flows and assessing the model's ability to replicate a credit program's performance."

SBA incurred far greater defaults under the SBIC PS program than were anticipated in its budgetary baselines, because of the substantial economic downturn experienced by the venture capital industry in recent years. As a result of these higher default levels, SBA performed a portfolio analysis and increased the expert opinion default assumptions and decreased the recovery assumptions used in the FY 2003 re-estimate cash flow model. SBA did not, however, revise its methodology or assumptions to reduce forecasts for reimbursements of prioritized payments or profit sharing in light of its increased net default projections and market volatility. Although SBICs are required to pay all leverage, reimbursements of prioritized payments may only be repaid out of profits, making reimbursement from defaulted SBICs unlikely. Both prioritized payments and profit sharing are material cash inflows that reduce the subsidy cost of the program.

In addition, SBA's projections of reimbursed prioritized payments appear unreasonable when compared to actual amounts that SBA experienced in prior years. We have concerns about the appropriateness of the outstanding leverage basis that was selected to forecast reimbursement of prioritized payments, as well as the method SBA used to calculate and apply its reimbursement curves. We recalculated reimbursement curves using the same outstanding leverage base and obtained a materially different result.

SBA's projections for profit-sharing participation are based on the SBICs' portfolio values (underlying investments). SBA is only entitled to a certain percentage of a profitable SBIC's return on investment. It did not appear that SBA reviewed its current projections for profit participation in light of the increase in net actual and projected defaults under the program. We noted that in the past 3 years, SBA's projection for profit sharing was materially greater than actual amounts received.

Recommendation

We recommend that the CFO:

1I. Determine if selection and development of the model's forecast assumptions are consistent with program guidelines and are reasonable in light of historical experience and current economic conditions and document the basis for such assumptions.

PROCEDURES TO ENSURE THE ACCURACY OF INPUTS AND OUTPUTS FOR THE CREDIT SUBSIDY CALCULATOR AND CONSOLIDATED CREDIT TOOLS

SBA did not have adequate controls to review and validate the accuracy of information input into the OMB Credit Subsidy Calculator (CSC), used to calculate the re-estimated subsidy rate and weighted average or single effective discount rate, and the Consolidated Credit Tool (Ccredit Tool), used to calculate the dollar amount of subsidy re-estimates and interest on re-estimates.

As part of the annual financial statement reporting process, SBA develops re-estimates for its material credit programs. It uses computer-based models to produce forecasted cash flows. The forecasted cash flows along with actual cash flows to date are then transferred to a spreadsheet (cash flow spreadsheet) suitable for use with CSC. The cash flow spreadsheets contain critical information necessary to calculate a proper re-estimated subsidy rate, such as the cohort year, convention for determining the discount rate ("use all" versus "90 percent"). In addition, SBA must update the CSC annually to reflect the most current actual versus budget assumption interest rates.

We noted that SBA's cash flow spreadsheets for the Section 7(a) business, Disaster Assistance, and SBIC programs contained errors. In addition, SBA did not update CSC for the most current interest rates before calculating some of its re-estimates.

SBA also uses the Ccredit Tool to calculate the subsidy re-estimate and interest on re-estimates for SBA's material credit programs. The following information, obtained from several sources, is input into the Ccredit Tool worksheets by SBA:

- Prior-year re-estimates (apportioned)
- Program disbursements
- Original (execution) subsidy rates

- Revised (re-estimate) subsidy rates from CSC
- Single effective interest rates from CSC

We noted that SBA made input errors, including incorrect disbursement amounts, incorrect re-estimated subsidy rates, and incorrect single effective discount rates.

As a result, SBA had at least two and sometimes three versions of re-estimates for various programs and/or cohorts within a program; changes were material to SBA's total re-estimates and impacted delays encountered in preparing timely financial statements. The problems stem from human error in performing a relatively detailed function and the lack of an effective quality assurance review process.

OMB Circular A-123, Management Accountability and Control, provides that:

> "…agencies and individual federal managers must take systematic and proactive measures to develop and implement appropriate, cost-effective management controls…."

Recommendation

We recommend that the CFO:

1J. Instruct the Office of Financial Analysis to develop a quality assurance review process (to be included in SBA's standard operating procedures) to minimize errors in calculating re-estimates and/or ensure that errors that do occur are detected and corrected in a timely manner. The review process should include steps to document validation results by noting that correct information has been reviewed and accepted, and that errors have been identified, corrected, and revalidated until ultimately accepted.

PROCEDURES TO IDENTIFY AND EXPLAIN UNUSUAL SUBSIDY BALANCES

SBA cannot fully support the reasonableness of its valuations for Credit Program Receivables and Related Foreclosed Property, Net and Liabilities for Loan Guarantees, for its 504, SBIC PS, Section 7(a), and Disaster Assistance programs. We performed an analysis of the present value of future cash flows in the underlying accounting records and noted account balances that do not appear plausible given (1) the nature of the particular program, (2) the program subsidy rates (re-estimated), and (3) the discounted present value of cash flow projections contained in the computer-based models. We noted material differences for the programs listed above.

SFFAS No. 2, states:

> "Direct loans disbursed and outstanding are recognized as assets at the present value of their estimated net cash inflows. The difference between the outstanding principal of the loans and the present value of their net cash inflows is recognized as a subsidy cost allowance."
>
> "For guaranteed loans outstanding, the present value of estimated net cash outflows of the loan guarantees is recognized as a liability."
>
> "These standards should apply to a cohort (or risk category) of direct loans or loan guarantees in the aggregate."

Tech Release No. 3 states:

> "The agency should review trends in the direct loan subsidy allowance account balance and/or the liability for loan guarantees account balance as compared to the outstanding balances of loans and/or guarantees. Any unusual fluctuations identified should be investigated and explained. When unusual fluctuations occur, an analysis by cohort may be helpful to identify the causes."

SBA devoted substantial resources and made noteworthy accomplishments in developing, implementing, and testing a revised approach to estimating cash flows for the Disaster Assistance program. In short, the modeling methodology effectively builds on available Disaster Assistance program data and takes a long-term view on performance through time. In addition, the approach supports the separate estimation of cash flows associated with loans sold and remaining loans and takes into account original term to maturity and other characteristics that influence program costs. As a result, SBA was able to restate the loss incurred under its asset sales program and more reasonable calculate subsidy re-estimates. In addition, the model output facilitates an analysis of the direct loan subsidy allowance account balance as compared to outstanding loan principal balances.

SBA began such an in-depth analysis of its Disaster Assistance program financing account balances, but did not provide similar analyses for its other credit programs. Although the Disaster Assistance program analysis proved meaningful, SBA fell short of completing it in time to produce its financial statements. In fact, SBA identified an important inconsistency in the application of credit reform concepts that creates a disconnect between outputs from its subsidy models, which assume transactions at one interest rate, and transactions recorded in its accounting system, which are calculated using a different interest rate. SBA recorded a $128.7 million adjustment to its Allowance for Subsidy Account to account for this inconsistency.

While much progress has been made, additional efforts are needed. SBA should develop a well-defined process that includes appropriate and systematic analyses, involving a broad array of OCFO and program managers, to continue to critique model results and reconcile results to the underlying accounting data embodied in the financial statements and footnotes. The process should be such that it can be performed for all programs routinely or at least annually when re-estimates are made.

Recommendations

We recommend that the CFO:

1K. Direct a coordinated effort among applicable OCFO branches, including the Office of Financial Analysis and the Office of Financial Administration, to identify potential disconnects between the agency's subsidy models and accounting records. Based on review results, make refinements to subsidy models and post correcting entries to the general ledger as appropriate.

1L. Implement a system of internal control in which the Office of Financial Analysis and the Office of Financial Administration monitor the direct loan subsidy allowance account balance (Account 1399) and the liability for loan guarantees account balance (Account 2180) as compared to the outstanding balances of loans and/or guarantees, at the program and cohort levels monthly. Maintain documentation that (a) explains unusual fluctuations determined to be appropriate, (b) supports any adjusting entries to the general ledger and (c) details revisions made to subsidy models and/or assumptions.

1M. Ensure that the Financial Reporting Information System (FRIS) general ledger and subsidiary feeder systems are properly accounting for credit reform activities at the program and cohort levels in accordance with SFFAS No. 2.

2. FINANCIAL MANAGEMENT AND REPORTING CONTROLS

SBA's financial management and reporting lack key controls, as follows:

- SBA management did not meet milestone dates and required excessive time to address audit questions
- Draft financial statements were unauditable.
- Funds control management needs improvement.
- Antideficiency Act internal control needs improvement.
- Prompt Payment Act control was inadequate.

We discuss SBA's substantial control weaknesses on the following pages under their respective captions.

SBA MANAGEMENT DID NOT MEET MILESTONE DATES AND REQUIRED EXCESSIVE TIME TO ADDRESS AUDIT QUESTIONS

SBA was unable to provide its FY 2003 draft financial statements and footnotes, the supporting trial balance, and key audit evidence in a timely manner. SBA's inability to meet agreed-upon milestone dates, submit timely and complete responses to our requests, and produce auditable draft financial statements in a timely fashion were, in part, a direct cause of our disclaimed opinion.

OMB Circular A-127, *Financial Management Systems,* states:

> "The agency financial management system shall be able to provide financial information in a timely and useful fashion to…comply with internal and external reporting requirements, including, as necessary, the requirements for financial statements prepared in accordance with the form and content prescribed by OMB and reporting requirements prescribed by Treasury."

As stated earlier, SBA made noteworthy accomplishments in developing and testing three new subsidy models and enhancing others during FY 2003. SBA was not able, however, to meet all of its own planned completion dates. As a result, SBA either could not perform or lacked due care in applying essential quality assurance procedures within its financial reporting environment. Once behind schedule, SBA could not respond to audit inquiries and follow-up requests for additional documentation in a timely manner. SBA's inability to provide adequate audit evidence was pervasive and prohibited us from completing our audit in accordance with auditing standards.

SBA's quality control procedures need major improvements in light of difficulties experienced in completing the FY 2003 financial statements and accelerated deadlines for submitting interim and final FY 2004 financial statements to OMB. SBA's quality control improvements must include controls for resource management to ensure that sufficient resources with the requisite qualifications and skill sets are assigned to the critical quality assurance tasks. In addition, SBA management must implement a well-thought-out critical-path approach for assessing timeframes for completing reconciliations; calculating accruals, re-estimates, and other manual adjustments; and closing the general ledger so that accurate financial statements can be prepared in time to complete appropriate analytical procedures and evaluate fluctuations in account balances.

Recommendation

We recommend that SBA's Administrator, in conjunction with the CFO:

2A. Assess whether SBA has devoted sufficient and qualified resources to adequately address its current financial reporting shortcomings and determine if the current process is in need of re-engineering to meet accelerated financial reporting deadlines in future years.

We also recommend that the CFO:

2B. Develop a comprehensive plan with firm milestone dates to meet the FY 2004 accelerated financial reporting date of November 15th.

DRAFT FINANCIAL STATEMENTS WERE UNAUDITABLE

SBA maintained insufficient and ineffective quality control over its December 22, 2003, draft Performance and Accountability Report. The report contained numerous, pervasive, and obvious errors involving inconsistency among the principal financial statements, footnote disclosures, required supplementary information (Intragovernmental Assets and Liabilities), and required supplementary stewardship information.

OMB Circular A-127, *Financial Management Systems,* states:

> "The agency financial management system shall comply with internal and external reporting requirements, including, as necessary, the requirements for financial statements prepared in accordance with the form and content prescribed by OMB and reporting requirements prescribed by Treasury."

The December 22, 2003, draft financial statements were unauditable for the reasons discussed below, among others. SBA submitted revised financial statements on January 9 and 16, in which most of the issues and concerns identified during our review were corrected. In some instances, however, we were precluded from reviewing the corrections due to time constraints.

Subsidy Re-alignment Entry

SBA recorded an off-line journal entry to properly align subsidy costs between Balance Sheet line items *Liabilities for Loan Guarantees* and *Credit Program Receivables and Related Foreclosed Property, Net*, for defaulted loan principal; it was improperly valued by a known amount of $61.9 million, because the underlying analysis to prepare the entry contained numerous errors as detailed below:

- The analysis for the Section 7(a) program estimated potential recoveries in excess of the total recovery rate resulting in an understatement to Account 1399, *Allowance for Subsidy*, of $15.5 million.

- The analyses for the Section 7(a), 504, and SBIC programs did not use the lesser of outstanding principal balances at September 30, 2003, or estimated recoveries remaining, as the result of cell reference errors, resulting in an understatement to Account 1399 of $46.4 million.

- Data used in the analysis to compute recoveries to date for the Section 7(a) and 504 programs were incomplete as the result of exclusion of asset sale proceeds (treated as recoveries) of $65 and $16.9 million, respectively. In addition, the Section 7(a) analysis included invalid loan sale activity in the recovery categories "Collections" (increase recoveries) and "Expenses" (reduce recoveries) of $63 million and $375 million respectively. In summary, recoveries as of September 30, 2003, included in the analysis were understated by $377 million for Section 7(a) and $16.9 million for 504. We did not quantify the misstatement resulting from use of improper data.

SBA provided a revised analysis; we did not have sufficient time to audit the revised analysis and resulting accounting entries or determine the magnitude of misstatements on the financial statements.

These widespread errors occurred because the Office of Financial Analysis did not take measures to ensure that data used in the analysis were complete, accurate, and appropriate for the purpose. Although SBA applied quality assurance procedures to the analysis, they were not comprehensive or effective to detect such errors before SBA recorded the transactions in its accounting system.

Loan Sale Reversal Entries

SBA reversed its prior-year loan sale audit adjustments in error, which created an understatement of $148 million on the Statement of Budgetary Resources line items *Spending Authority from Offsetting Collections* and *Obligations Incurred*. SBA did not have a process in place to detect this error.

Disaster Re-estimate Misstated

SBA's disaster loan re-estimate was improperly recorded in the general ledger, resulting in misstatements on the December 22, 2003, draft financial statements as follows:

Account	Issue Description	Overstated Amount
7401 – Prior Period Adjustment	Prior Period Adjustment overstated due to an improper entry (Debit instead of Credit entry)	$996 million
5105U – Subsidy Expense Unfunded	Entire Modification Adjustment Transfer was recorded in FY 2003, instead of applicable sale years.	FY 2001 = $97 million FY 2002 = $55 million FY 2003 = $28 million
7401 – Prior Period Adjustment	OCFO did not reverse its previously recorded FY 2001 re-estimates in the accounting system	$509 million

SBA's quality assurance review procedures were inadequate and did not detect these errors either before or after the re-estimate transactions were recorded in the accounting system.

As noted earlier, SBA determined that its interest expense payable to Treasury has been consistently overstated since the inception of credit reform as the result of inconsistencies between various credit reform tools and schemes for calculating cohort weighted average or single effective interest rates. SBA recorded a $128.7 million adjustment to correct for these inconsistencies; it recorded the adjustment as a current-year re-estimate rather than as a current- and prior-period adjustment to interest expense payable to Treasury. As a result, Subsidy Expense and Interest Expense are overstated.

Inadequate Disclosures Associated with FY 2002 Restatements

SBA's footnote disclosures in its December 22, 2003, draft financial statements related to FY 2002 restatements for prior-period adjustments did not sufficiently describe the nature of errors in previously-issued financial statements.

During FY 2003, 12 issues were identified that required restatement of the FY 2002 comparative year balances. SBA's quality assurance procedures were not adequate to ensure that disclosures were meaningful, accurate, and sufficient in accordance with generally accepted accounting principles. To illustrate, SBA characterized an $800 million restatement related to the Disaster Assistance program's allowance for subsidy as: "The SBA corrected some flaws in its Disaster model for FY 2002."

SFFAS No. 21, *Reporting Corrections of Errors and Changes in Accounting Principle* states:

> "The nature of an error in previously issued financial statements and the effect of its correction on relevant balances should be disclosed."

Insufficient footnote disclosure related to prior-period adjustments impairs the usefulness of financial statements and may mislead those who rely on disclosures contained within.

Restated Gain or Loss on Asset Sales

SBA conducted an analysis to calculate revised gain/loss on loans sold during FYs 1999 through 2003. SBA computed a revised net book value using various assumptions depending on the program and available data. The revised net book value was subtracted from the loan sale proceeds to calculate a revised gain/loss. We noted concerns with the data used in this analysis for the 7(a) and 504 guaranteed business loan programs and communicated our concerns to management. Although SBA acknowledged an error in part of its analysis, the error did not affect the revised gain/loss reported in the December 22, 2003, draft financial statements, in which it disclosed $163 million and $126 million changes between previously reported losses and revised gains in its Section 7(a) and 504 credit programs.

No Allowance for Subsidy for SBIC Prioritized Payments

SBA did not have a process in place to identify the need for a valuation adjustment related to SBIC prioritized payments and thus omitted this material adjustment from its December 22, 2003, financial statements. SBA's failure to realign subsidy cost related to prioritized payments overstated *Credit Program Receivables* and *Related Foreclosed Property, Net.* SBA developed a methodology and prepared a material adjustment; we did not have sufficient time to evaluate the methodology or resulting accounting entries designed to correct the problem.

Secondary Market Guarantee Liability was Inaccurate

SBA included a preliminary estimate of the net present value of future cash flows related to the Secondary Market Guarantee program in its December 22, 2003, draft financial statements ($93 million). The revised estimate ($148 million) was not finalized until January 9, 2004, which did not allow us sufficient time to evaluate it.

Untimely Charge-off of Loans Receivable

SBA maintains purchased Section 7(a) loans that have been discharged in bankruptcy on its books at full (net book) value until SBA is able to conclude that it has no recourse against guarantee lenders. This practice overstates the valuation of the following two components of footnote number 6, *Credit Program*

Receivables and Related Foreclosed Property, because SBA does not have recourse against lenders in most instances.

- Defaulted Guarantee Loans Receivable, Gross
- Allowance for Subsidy Cost

Our random sample of all loans identified one loan matching the above condition. While our sampled loan transaction was not in itself material to the financial statements, the statistically-projected error had a material effect on SBA's footnote components. Generally accepted accounting principles require all economic events that have occurred to be recorded and reflected in the financial statements.

Recommendations

We recommend that the CFO:

2C. Design specific procedures to identify accounts requiring estimation or other adjustment in a timely manner to achieve proper valuation in the financial statements.

2D Lead a collaborative effort between the Office of Financial Administration accountants and the Office of Financial Analysis analysts, such that sufficient knowledge transfer is achieved to enable SBA to design and implement comprehensive and effective analyses and review processes regarding estimates and other accounting adjustments.

2E Complete the document titled *Checklist for Reports Prepared Under the CFO Act--Revised 2003*, as issued jointly by the General Accounting Office and the President's Council on Integrity and Efficiency, before submitting financial statements to help ensure the adequacy of financial statement presentation and disclosure.

FUNDS CONTROL MANAGEMENT NEEDS IMPROVEMENT

SBA's funds control management needs improvement because of two shortcomings. First, SBA is not detecting and correcting invalid *Budget Proforma* (defined below) entries. Second, SBA is not effectively monitoring undelivered orders (UDOs).

Invalid Budgetary Pro-Forma Entries

SBA uses an application called the *Budget Proforma* to record budgetary accounting entries based upon proprietary and memorandum transactions occurring in LAS. SBA uses this application, because LAS does not include budgetary accounting transactions.

SBA's budget proforma application uses improper posting logic; in addition, SBA management failed to review resulting transactions. These shortcomings resulted in numerous misstatements on the combined statement of budgetary resources, as discussed below.

Transaction Code 260 Produces Inaccurate Results

For LAS transaction code 260, Payment of Asset Sale Cost, SBA established two proprietary accounts (asset and liability) that when netted, approximates the UDO for asset sale administrative cost anticipated, but not incurred. These proprietary accounts are unnecessarily included in the budget proforma, thus creating erroneous budgetary entries. As noted in our FY 2002 audit report, SBA failed to detect this error. During FY 2003, the asset and liability accounts were reversed, again creating erroneous budgetary entries. Again, SBA failed to identify and correct the invalid entries, causing the Statement of Budgetary

Resources line items *Spending Authority from Offsetting Collections* and *Obligations Incurred* to be understated by $138 million. SBA posted correcting entries after we brought the errors to its attention.

Liquidating Fund Transactions

SBA improperly posted accounting transactions in its liquidating fund due to invalid budget proforma posting logic. As a result, third-quarter Statement of Budgetary Resources line items were misstated as follows:

Line Item	Nature of Error	Overstated Amount
Recoveries of Prior Year Obligations	SBA recorded recoveries of prior year obligations based upon underlying transactions that were not obligations.	$12 million
Obligations Incurred	SBA recorded upward adjustments of prior year obligations based upon underlying transactions that were not obligations.	$5 million
Net Transfers	SBA utilized an improper Standard General Ledger (SGL) account to record repayments of debt to the Federal Financing Bank (FFB), resulting in payments being classified as *Net Transfers* instead of *Permanently Not Available*.	$20 million

SBA posted adjusting entries to correct misstatements noted above, which were reflected in its December 22, 2002, financial statements.

Substantial compliance with the SGL at the transaction level, as mandated by the Federal Financial Management Improvement Act (FFMIA), requires that SBA record financial events consistent with applicable posting models/attributes reflected in the SGL. Generally accepted accounting principles require that transactions be recorded based upon events that actually occurred.

Monitoring Undelivered Orders

SBA's monitoring of UDOs needs improvement to address control deficiencies, as discussed below:

Invalid Disaster Assistance Program Loan Financing Fund Undelivered Orders

Outstanding disaster loan approvals represent UDOs in SBA's disaster loan financing fund. We tested 83 outstanding disaster loan UDOs established before FY 2003 and determined that 61 (or 74 percent) were invalid at September 30, 2003. These invalid UDOs overstated the statement of budgetary resources line item *Undelivered Orders by* $3.2 million.

The 61 invalid UDOs were the result of:

- Duplicate loan approvals entered in the accounting system (36).
- Invalid posting logic, which created UDOs when SBA cancelled borrower checks (9).
- Failure to de-obligate un-needed obligations in a timely manner (16).

OMB Circular A-11 defines a valid obligation as a binding agreement that will result in outlays, immediately or in the future. The UDOs detailed above would not have been liquidated via outlay in the future.

Administrative Undelivered Orders Overstated at Year End

SBA maintained invalid or unneeded administrative UDOs in its general ledger, because they were not liquidated in a timely manner as the result of improper cut-off procedures, and SBA did not deobligate unneeded obligations. In addition, SBA was unable to provide support for one recorded administrative UDO. Consequently, administrative UDOs as of September 30, 2003, are overstated by a known amount of $178,110 and a projected amount of $52,836,526. As a result, the following financial statement line items are misstated:

Financial Statement	Line Item	Effect	Amount
Budgetary Resources	*Undelivered Orders*	Overstated	$53 million
	Accounts Payable	Understated	$20 million
	Unobligated Balances	Understated	$33 million
Net Cost	*Gross Costs*	Understated	$20 million
Balance Sheet	*Accounts Payable*	Understated	$20 million
Changes in Net Position	*Appropriations Used-Cumulative Results*	Understated	$20 million
	Appropriations Used-Unexpended Appropriations	Understated	$20 million

Generally accepted accounting principles require that all economic events that occur in the current period be recorded in the current period.

This condition was attributable to SBA's inability to provide adequate supporting documentation to substantiate one UDO and the following SBA control weaknesses:

- Noncompliance with Year-End Closing Instructions to properly monitor existing obligations for inactivity or continuing need.

- No system (except for grant accruals) to accrue for goods and services received and not yet invoiced as of September 30.

Recommendations

We recommend that the CFO:

2F. Correct known budgetary proforma errors and perform a complete analysis of posting logic to ensure compliance with the SGL at the transaction level.

2G. Coordinate with the Office of Disaster Assistance to develop and implement procedures to review and determine the validity of outstanding disaster Loan UDOs quarterly. Invalid UDOs should be de-obligated to ensure efficient use of funds.

2H. Coordinate with the Director of the Office of Procurement and Grants Management to develop additional or strengthen existing internal controls to identify administrative obligations with no activity and process de-obligations in a timely manner.

2I. Develop procedures to ensure proper cut-off to ensure completeness of administrative transactions for financial reporting.

2J. Ensure that adequate supporting documentation is maintained to substantiate recorded administrative obligations.

ANTIDEFICIENCY ACT CONTROL NEEDS IMPROVEMENT

SBA's controls to ensure compliance with the Antideficiency Act need improvement, because management did not detect the potential violations discussed below.

Expired Salary and Expense Funds

SBA does not have sufficient funds control to ensure that activity affecting expired salary and expense funds is valid and does not result in Antideficiency Act violations. This is evidenced by the fact that SBA had obligation activity in expired funds during FY 2003 that could not be explained in a timely fashion by SBA management.

OMB A-11, *Preparation, Submission, And Execution of the Budget,* states that agencies may "disburse against obligated balances and adjust obligated balances to reflect actual obligations during the period of availability."

SBA posted invalid administrative recoveries of prior-year obligations and obligations incurred due to the correction of vendor administrative data for existing obligations and the transfer of summary-level obligations to the organizational level within its administrative general ledger. The deobligation of valid prior-year obligations created recovery transactions that map to the combined Statement of Budgetary Resources line item *Recoveries of Prior Year Obligations.* The subsequent re-establishment of the obligations created a transaction that mapped to the line item *Obligations Incurred*. These invalid transactions overstate the above line items by a known total of $10 million. In addition to creating financial statement misstatements, these invalid postings created new obligations in expired funds, giving the appearance of Antideficiency Act violations. SBA did not have a process in place to identify this potential Antideficiency Act violation and only investigated this activity upon our request.

While management was able to determine that the invalid activity noted above did not cause an Antideficiency Act violation, there were additional postings to expired funds for which SBA was unable to provide sufficient detail. Consequently, we could not conclude if Antideficiency Act violations occurred.

Journal Vouchers in FRIS

During FY 2003, SBA developed and implemented a manual system of control to ensure that routine loan-related transactions (i.e. default claim payments) did not exceed the lesser of cash available (in the relevant fund) or realized apportioned authority. This manual system of control is inadequate, because it does not ensure against potential Antideficiency Act violations. An example follows.

SBA recorded an adjustment via journal voucher to increase obligations incurred to offset the invalid budgetary effects created by SBA's practice of tracking loan sale related administrative costs (transaction code 260). A portion of this invalid effect ($17 million) had already been corrected before the adjustment was recorded, thus the adjustment overstated the obligations incurred line item by $17 million. This created a situation in which obligations incurred in Fund X4154 exceeded apportioned authority in the fund. This invalid obligation and resulting potential Antideficiency Act violation were not detected by

SBA until we presented the results of our Antideficiency Act compliance test work. At that time, correcting entries were posted to properly state obligations incurred in Fund X4154.

Recommendations

We recommend that the CFO perform the following for administrative funds:

2K. Continue to review obligation activity posted against expired funds in FY 2003 and make a determination if the Antideficiency Act was violated. Maintain sufficient documentation to ensure a clear audit trail during FY 2004.

2L. Develop control techniques to ensure that only valid obligation activity is posted against expired funds and review transactional detail monthly to ensure no invalid activity was posted.

We also recommend that the CFO perform the following for loan funds:

2M. Investigate the possibility of implementing automated funds controls that allot the lesser of apportioned authority or realized resources at the fund level.

2N. Enhance its cash management tracking system by implementing a control technique to ensure that obligations incurred transactions entered via journal voucher do not exceed the lesser of apportioned authority or realized resources.

PROMPT PAYMENT ACT CONTROL WAS INADEQUATE

SBA does not pay interest on late payments (those over 30 days) to vendors that it has identified in its accounting system as "immediate pay." We identified four FY 2003 payments that did not include the interest penalty due on amounts paid late, because the vendor was identified as immediate pay.

In its accounting system, SBA denoted a number of vendors to receive payment for goods and services immediately; instead of waiting 30 days—the delay typically transpiring before Prompt Payment Act interest is required—and has designated all such vendors as immediate pay in the accounting system. SBA considers these vendors to have waived their rights to interest on late payments. These vendors, however, are not always paid within the 30-day prompt payment period, and they do not appear to have authorized or approved either SBA's immediate pay designation or SBA's withholding of interest on late payments because of this designation.

U.S. Code Part 1315.4(h) *Prompt Payment Standards and Required Notices to Vendors*, requires that "when payments are made after the due date, interest will be paid automatically.…" SBA is not paying interest due to these vendors and is not complying with the Prompt Payment Act.

Recommendation

2O. We recommend that OCFO calculate and pay all interest due to immediate pay vendors for late payments in prior fiscal years. We also recommend that SBA begin paying Prompt Payment Act interest to these vendors on future late payments.

INADEQUATE CONTROL OVER ACCOUNTING ENTRIES RELATED TO TRANSACTION CODE 195

SBA's proforma accounting entries and financial statement reporting related to guarantee loan purchases (transaction code 195) resulted in departures from SGL posting logic and federal accounting standards with respect to determining the valuation of liabilities. Misstatements of interest revenue and default cost equaled $65 million in FY 2002 and $58 million in FY 2003, and the liability was overstated by about $25 million.

Transaction code 195 incorrectly debits a revenue account (SBA Account 4020, Interest Income on Loans Receivable) at the time of purchase. This represents a cash outflow or program cost to reimburse the lender for accrued interest from the borrower at the time of default. SBA's account 4020 crosswalks to SGL account 5310, Interest Income - Loans Receivable; the debit transaction understates total interest revenue and understates total default costs.

In addition, transaction code 195 establishes a claim payable (SBA account 2832 – Due Bank Disallowed Purchased Interest) to guarantee lenders for disallowed purchased interest (accrued interest typically greater than 180 days) at 100 percent of the claim value. Contractually, these claims are only payable to lenders if the loan reaches paid-in-full status. Historical experience has shown that claims paid to lenders related to disallowed interest are far less than 100 percent.

SBA does not have a quality-assurance process in place to detect instances in which its accounting is not SGL compliant or its account balances are valued improperly or misstated. At our request, SBA established a valuation methodology to estimate the value of future claim payments for disallowed purchased interest and reflected adjustments in its accounting system for FY 2002 restated yearend balances and FY 2003 balances beginning in the third quarter.

Recommendation

We recommend that the CFO:

2P. Perform a thorough account analysis at the fund level to identify account and posting anomalies, such as accounts with unnatural balances. Any anomalies detected should be researched and subsequently corrected to ensure compliance with SGL posting logic and federal accounting standards.

3. AGENCY-WIDE INFORMATION SYSTEMS CONTROLS

SBA continued to improve internal control over its information system environment during FY 2003 in certain areas. Specifically, SBA:

- Conducted certification and accreditation (C&A) reviews for additional major applications.
- Continued to implement the Windows 2000 operating system at various field locations.
- Completed corrective actions to close 20 prior-year recommendations.

These accomplishments were, however, overshadowed by:

- Delays in timely implementation of corrective actions to resolve prior-year weaknesses by SBA's program offices.
- Implementation of ineffective controls to address previously-identified weaknesses.
- Inadequate participation by OCIO in the development of new systems to ensure that system security controls are addressed effectively and in a timely manner and to ensure that systems meet goals, objectives, and requirements of federal laws, regulations, and standards.
- Inadequate allocation of resources to support OCIO's security program.

SBA's OIG will issue a separate report titled *Audit of SBA's Information System Controls, FY 2003,* that will detail scope of work in the following categories:

General Control Categories

- Entity-wide security program control
- Access control
- Application software development and program change control
- System software control
- Segregation-of-duty control
- Service continuity control

Application Control Categories (Oracle administrative accounting system)

- Authorization control
- Completeness control
- Integrity of processing and data file control
- Accuracy control

The OIG's report will convey our findings and recommendations in these areas.

STATUS OF PRIOR-YEAR FINDINGS

As required by *Government Auditing Standards*, we provide the status of reportable conditions for the prior-year audit.

Description	Recommendation	Status
Disaster Loan Program Modeling	Revise the approach to estimating cash flows for the disaster loan program. (1A)	Implemented.
	Ensure that the Office of Financial Analysis adheres to documentation requirements of Federal Financial Accounting and Tech Release No. 3. (1B)	Partially Implemented.
Liability for Loan Guarantees and Related Accounts for Pre-1992 Loan Commitments	Estimate the Pre-1992 guarantee loan default liability utilizing risk factors in accordance with SFFAS No. 2. Maintain documentation. Perform analysis to assure estimate conforms to SFFAS No. 2. (2)	Implemented.
Financial Reporting	Assess whether SBA has devoted sufficient resources to adequately address its current financial reporting, and decide if it should be re-engineered. (3A)	Unresolved. Repeat Recommendation.
	Perform fluctuation analyses and correct obvious errors before submitting draft financial statements. (3B)	Unresolved. Revised Recommendation.
	Re-engineer and enhance the quality control process and continue to develop and document the financial reporting process. (3C)	Unresolved. Revised Recommendation.
Funds Control	Review obligated and unobligated balances remaining in liquidating funds. Deobligate where appropriate. (4A)	Implemented.
	Develop and implement an integrated funds control system. (4B)	Unresolved. Revised Recommendation.
	Develop and implement a process to record apportionment amounts accurately. (4C)	Implemented.
Master Reserve Fund	Develop a process for estimating SBA's ownership in earnings from the MRF that provided accurate, complete, and timely data for the financial statements. SBA's process should at least include a representative statistical sample to estimate the gain or loss on closed pools and extrapolation of such results, taking into account any differences in characteristics between closed and open pools. (5A)	Implemented.
Agency-wide Information Systems Control	Please refer to separate report.	Unresolved. Updated in Separate Report.

OTHER MATTERS

We considered SBA's internal control over required supplementary stewardship information by obtaining an understanding of SBA's internal control, determining if internal control had been placed in operation, assessing control risk, and performing tests of control as required by OMB Bulletin No. 01-02. Our objectives were not to provide assurance on internal control; accordingly, we do not provide an opinion on such control.

Finally, with respect to internal control related to SBA performance measures, we obtained an understanding of the design of significant internal control relating to existence and completeness assertions, as required by OMB Bulletin No. 01-02. We concluded that SBA's control over performance measures must be enhanced to ensure accuracy and reliability as required by OMB Bulletin 01-09 and prevailing FASAB standards. Our procedures were not designed to provide assurance on internal control over reported performance measures; accordingly, we do not provide an opinion on such control.

We also noted certain other matters involving internal control that we will report to SBA management in a separate letter.

This report is intended solely for the information and use of SBA management, OMB, and Congress, and is not intended to be and should not be used by anyone other than these specified parties.

Very truly yours,

COTTON & COMPANY LLP

Charles Hayward, CPA
Partner

January 28, 2004
Alexandria, Virginia

COTTON & COMPANY LLP
auditors • advisors
DAVID L. COTTON, CPA, CFE, CGFM • CHARLES HAYWARD, CPA, CFE, CISA • MICHAEL W. GILLESPIE, CPA, CFE • CATHERINE L. NOCERA, CPA, CISA
MATTHEW H. JOHNSON, CPA, CISA, CGFM • SAM HADLEY, CPA, CGFM • COLETTE Y. WILSON, CPA • ALAN ROSENTHAL, CPA • LOREN SCHWARTZ, CPA, CISA

Independent Auditor's Report on Compliance with Laws and Regulations

Inspector General
U.S. Small Business Administration

We were engaged to audit the financial statements of the U.S. Small Business Administration (SBA) as of and for the years ended September 30, 2003, and 2002, and have issued our report thereon, dated January 28, 2004, in which we disclaimed an opinion on those financial statements.

SBA management is responsible for complying with laws and regulations applicable to the agency. Except as noted in the following paragraph, we performed tests of SBA's compliance with certain provisions of laws and regulations, noncompliance with which could have a direct and material effect on the determination of financial statement amounts, and certain other laws and regulations specified in Office of Management and Budget (OMB) Bulletin 01-02, *Audit Requirements for Federal Financial Statements*, including requirements referred to in the Federal Financial Management Improvement Act (FFMIA) of 1996. We limited our tests of compliance to these provisions and did not test compliance with all laws and regulations applicable to SBA.

Our Independent Auditor's Report on Internal Control describes, under the caption SBA Management Did Not Meet Milestone Dates and Required Excessive Time to Address Audit Questions, a number of conditions that adversely impacted the scope of our work. These conditions precluded us from completing our testwork of SBA's compliance with the Antideficiency Act.

Results of our tests of compliance disclosed instances of noncompliance with the Prompt Payment Act that are required to be reported under *Government Auditing Standards* and OMB Bulletin 01- 02. Our Independent Auditor's Report on Internal Control describes this matter in detail and provides our recommendations for corrective action by SBA management.

Under FFMIA, we are required to report whether SBA's financial management systems substantially complied with federal financial management system requirements, federal accounting standards, and the United States Government Standard General Ledger (SGL) at the transaction level. To meet this requirement, we performed tests of compliance with FFMIA Section 803(a) requirements. Results of our tests disclosed instances, described below, indicating that SBA's financial management systems did not substantially comply with federal financial management system requirements, federal accounting standards, and the United States SGL at the transaction level.

Please see our Independent Auditor's Report on Internal Control (applicable section cited) for details regarding each of the matters discussed below.

C&C
established 1981
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SBA is not in substantial compliance with federal financial management system requirements, because:

- Its core financial system was not able to provide complete, reliable, timely, and consistent financial management information on programs to enable management to fulfill its responsibility to the public and provide timely financial information for preparing financial statements and footnotes and managing current operations, as required by OMB Circular A-127, *Financial Management Systems*. (SBA Management Did Not Meet Milestone Dates And Required Excessive Time To Address Audit Questions)

- Access control, segregation-of-duty, and other general-control weaknesses existed, which will be described in the Office of Inspector General report titled *Audit of SBA's Information System Controls, FY 2003*. (Agency-Wide Information Systems Control Environment)

- Security weaknesses and nonconformances with OMB Circular A-130, *Management of Federal Information Resources*, continued to exist in certain major applications and general support systems. (Agency-Wide Information Systems Control Environment)

- SBA maintained insufficient funds control over obligations entered via journal voucher in the Financial Reporting Information System (FRIS). (Antideficiency Act Control Needs Improvement)

SBA was not in substantial compliance with federal accounting standards, because it:

- Could not support the valuation of subsidy-related balances for the Disaster Assistance, 504, Small Business Investment Company, Participating Security and Section 7(a) loan programs. (Procedures to Identify and Explain Unusual Subsidy Balances)

- Improperly reversed prior-year audit adjustments, misstating current-year budgetary collection and disbursement activity. (Invalid Budgetary Pro-Forma Entries)

- Overstated loan and administrative undelivered orders at September 30, 2003, when it failed to deobligate unneeded obligations and properly accrue for goods and services received as of September 30, 2003. (Monitoring Undelivered Orders)

- Improperly valued the entry to realign subsidy costs from the consolidated balance sheet line item *Liabilities for Loan Guarantees* to *Credit Program Receivables and Related Foreclosed Property, Net* for defaulted guarantee loans. (Subsidy Realignment Entry)

- Recorded invalid budgetary transactions based upon improper budgetary posting logic for asset-sale administrative costs and liquidating fund transactions. (Invalid Budgetary Pro-Forma Entries)

- Improperly recorded Disaster Assistance program subsidy re-estimates. (Disaster Re-estimate Misstated)

- Disclosed insufficient detail about prior-period adjustments and credit subsidy matters. (Inadequate Disclosures Associated with FY 2002 Restatements)

SBA was not in substantial compliance with the United States Government SGL at the transaction level, because:

- Its combined statement of budgetary resources reflected line item misstatements resulting from failure to record Federal Financing Bank repayment transactions in accordance with SGL criteria. (Invalid Budgetary Pro-Forma Entries)

- SBA's program for posting budgetary transactions to FRIS (known as "Budget Proforma") which is based upon proprietary and memorandum events in the Loan Accounting System, recorded numerous transactions that did not comply with SGL posting logic. (Invalid Budgetary Pro-Forma Entries)

- SBA’s automated transaction code used to record default payments to guarantee lenders, improperly recorded purchased interest as contra revenue instead of an expense. This treatment understated program revenues and expenses. (Inadequate Control Over Accounting Entries Related To Transaction Code 195)

- SBA recorded invalid recoveries of prior-year obligations and obligations incurred as the result of conversion problems from its Federal Financial System to its current Oracle-based administrative accounting system. (Monitoring Undelivered Orders)

SBA’s Office of the Chief Financial Officer is responsible for financial management systems within SBA. SBA should assign priority to corrective actions for these FFMIA-related matters consistent with requirements of OMB Circular A-50, *Audit Followup*.

Providing an opinion on compliance with certain provisions of laws and regulations was not an objective of our work; accordingly, we do not express such an opinion.

This report is intended solely for the information and use of SBA management, OMB, and Congress and is not intended to be and should not be used by anyone other than these specified parties.

COTTON & COMPANY LLP

Charles Hayward, CPA

January 28, 2004
Alexandria, Virginia

CHIEF FINANCIAL OFFICER'S REPLY

DATE: January 23, 2004

TO: Robert Seabrooks, Assistant IG for Auditing

FROM: Thomas Dumaresq, Chief Financial Officer

SUBJECT: FY 2004 Financial Statement Audit Report

The Small Business Administration (SBA) is in receipt of the draft Independent Public Accountant (IPA) reports from Cotton and Company, LLP, that include the auditor's opinion and separate reports on internal controls and compliance with laws and regulations. As you know, the IPA audit of the Agency's financial statements and related processes is a core component of SBA's financial management program.

Unfortunately, the results of this year's audit process indicate that despite SBA's significant improvements over the past year, our efforts have not been sufficient to meet existing financial management standards. The auditor has indicated that it is unable to satisfy itself that the SBA's financial statements fairly present the financial position of SBA as of September, 2003 and 2002. The audit report states that because SBA was late in completing its budgeting and accounting work for certain credit programs and preparing its financial statements, the auditor did not have sufficient time to complete the auditing procedures necessary to form a reasonable basis of opinion on the statements.

SBA acknowledges that key milestone dates were not met and accepts responsibility for not providing sufficient time for the auditor to complete its work. The ambitious subsidy model development agenda we developed to address last year's audit findings ultimately required more time than was available, which left insufficient time for the SBA to complete its established quality assurance review process prior to the completion of the financial statements. Therefore, the draft financial statements delivered to the auditor on December 22nd did not have the benefit of our planned review process. Many of the issues included as audit findings were corrected in revised statements submitted on January 3rd. Pursuant to our agreement with Cotton, we submitted a third version of the financial statements on January 9th that included almost all of Cotton's audit findings as of December 22nd. The final statements submitted on January 16th did include a few additional changes recommended by Cotton at the time. SBA believes the final statements delivered on January 16th provide a fair representation of the Agency's financial condition including the restatement of fiscal 2002 results. Unfortunately, the auditor did not have sufficient time to complete its review of those materials.

Last year three key items were identified in the disclaimer opinion: the disaster loan and sales program cost estimates, the Master Reserve Fund Secondary Market Guarantee (MRF SMG) residual value estimate, and the liability for loan guarantees for pre-1992 loans. SBA developed new subsidy estimate models for the Disaster and the MRF/SMG programs as recommended by the auditor last year. The auditor's report acknowledges that the work was completed but indicates Cotton & Co. did not have sufficient time to review all of the relevant materials. We also addressed the pre-1992 loan guarantee issue, and Cotton & Co. was able to review that and agree that the issue had been resolved.

The IPA's Report on Internal Control identifies two material weaknesses: the credit reform control environment and the financial management and reporting control environment. The audit identifies numerous examples of inconsistencies and errors in our credit reform modeling and reporting environment. Many of these issues were contributing factors to the weaknesses in our financial management and reporting results. Overall, we agree with Cotton & Co.'s findings that we need better internal controls over these processes to ensure higher quality results. As noted above however, because of the subsidy model development and restatement related work that had to be completed this year, we were unable to conduct sufficient quality assurance prior to submitting our financial statements. We believe that if we had been able to carry out our quality assurance process as planned, our December 22nd financial statements would have been much better. Instead, it took us a few more weeks to reach that point, which was too late for our auditors to review.

For FY04, we will develop a comprehensive plan with firm milestone dates to meet the accelerated reporting date of November 15th. We will again assess whether we have committed adequate resources to the task. However, we believe that the work we did last year – building three new subsidy models, substantially modifying two others, and resolving major prior year restatement problems – will put us in a much better position this coming year. We anticipate doing only minor model development work this year which will allow us to focus more on our internal control and review processes. We look forward to the opportunity to actually fully implement our quality assurance review process in FY04 and believe that will make a major difference in addressing the types of errors and misstatements identified by Cotton & Co. this year.

We also agree with Cotton & Co.'s recommendation that we take steps to identify and understand unusual subsidy and related account balances. We did make substantial progress on this for the disaster program this year, but there is still work to be done, particularly for SBA's other loan programs. This will be a top priority for SBA in FY04.

Cotton & Co. also recommends improving our standard operating procedures and subsidy model documentation, doing more data reconciliation and quality assurance for the MRF SMG and the SBIC programs, and improving the estimation process for various loan accounts. These are all fundamentals of good financial management and SBA is committed to accomplishing as many of these items as possible in the coming year. Improving funds control management continues to be an issue for SBA. We made important strides in this area over the past year but we agree with Cotton & Co. that further improvements are necessary.

We appreciate all of your efforts and those of your colleagues in the Office of the Inspector General as well as those of Cotton & Co. While the audit process was again very challenging this year, we believe our efforts and the assistance we received from you and Cotton & Co. resulted in substantial improvements in the quality of our financial statements. Overall we feel our financial management capacity has improved considerably this year and we are proud of what we have accomplished. While we are disappointed that the audit results do not reflect an overall improved financial position for the Agency, we believe the work we completed this year was very significant and puts us in a strong position for the coming year. We continue to be committed to excellence in financial management and look forward to making more progress in the months ahead.

FINANCIAL STATEMENTS

This is the thirteenth year that the Small Business Administration (SBA) has issued agency-wide financial statements. The preparation of financial statements is a critical aspect of ensuring the accountability and stewardship for the public resources entrusted to the SBA. Preparation of these statements is also an important part of Agency financial management's goal of providing accurate and reliable information that may be used to assess performance and allocate resources.

These themes of accuracy and accountability resonate particularly strongly this year because of the extensive improvements that the Agency made to address the critical longstanding issues that were identified last year as undermining our ability to meet these core objectives in our financial accounting and reporting. Inconsistencies and weaknesses in the budgeting and accounting for the SBA's loan asset sale program were corrected. A new subsidy model was built for Disaster program costs and the statements and footnotes now accurately include the cost of the Disaster program and accurately present the results of the SBA's loan asset sale program.

In addition, the SBA updated its 7(a) econometric model that was first used for the FY 2003 budget. Also, the Agency updated the assumptions used for defaults and recoveries in its SBIC program models. Finally, the SBA built a new model for its 504 Development Company program that will be first used for the fiscal 2005 budget. The SBA completed this work through an aggressive approach that employed Agency as well as expert outside modeling experts. These changes were made in concert with the Office of Management and Budget (OMB). Also, extensive review and quality assurance was conducted on the new models including review by outside modeling experts.

The SBA also built a model to estimate the adequacy of the Master Reserve Fund (MRF) to fund the Secondary Market Guarantee to investor in 7(a) securities. Last year our independent auditor determined that the SBA did not furnish sufficient evidence to support the MRF liability in the financial statements, and this new model addresses this finding. Also, the Agency developed a new procedure to estimate the liability for guarantees for the pre-Federal Credit Reform business loan portfolio. The SBA has included the effects of these improvements in a restatement of its previous year's financial statements.

The responsibility for the accuracy and propriety of the information contained in the principal financial statements and the quality of internal controls rests with management. The financial statements have been prepared from the books and records of the Agency; however they differ from the financial reports used to monitor and control budget execution. Also, the Agency recognizes that it cannot liquidate liabilities not covered by budgetary resources without an enactment of an appropriation by the Congress and an apportionment by the OMB.

The principal financial statements have been prepared to report the financial position and results of operations of the entity, pursuant to the requirements of 31 U.S.C 3515 (b). These financial statements have been prepared in accordance with guidance issued by the OMB pursuant to the Chief Financial Officers (CFO) Act of 1990.

While the statements have been prepared from the books and records of the entity in accordance with generally accepted accounting principals (GAAP) for Federal entities and the formats prescribed by OMB, the statements are in addition to the financial reports used to monitor and control budgetary resources which are prepared from the same books and records.

The statements should be read with the realization that they are for a component of the U.S. Government, a sovereign entity.

Balance Sheet

The Consolidated Balance Sheet summarizes the assets, liabilities, and net position as of the end of the fiscal year. For clarity in presentation, assets and liabilities have been differentiated between those resulting from transactions between Federal entities (intragovernmental) and those resulting from transactions between the Agency and non-federal entities. Information for two years is presented for the purpose of comparison.

The SBA's total assets decreased $5.04 billion or 41% from $12.20 billion as of September 30, 2002 to $7.16 billion as of September 30, 2003. Fund Balances with Treasury decreased by $4.70 billion or 63% due to repayment of Treasury borrowings from SBA's Disaster Loan Program. Credit Program Receivables and Related Foreclosed Property decreased by $.30 billion due to assets sales. The SBA began selling pools of loans from its portfolios in 1999 instead of continuing to service the loans. A single sale was completed in 2000 and two sales were made in 2001 and 2002. The final sale was completed in 2003.

SBA's total liabilities decreased $3.61 billion or 26% from $13.94 billion as of September 30, 2002 to $10.33 billion as of September 30, 2003. Intragovernmental liabilities decreased by $4.83 billion due to a decrease in the amount owed to Treasury from borrowings. Total other liabilities – public increased by $1.21 billion due to a increase in the loan guarantee liabilities of the business programs.

SBA's net position consists of Unexpended Appropriations and Cumulative Results of Operations. Unexpended Appropriations reflects spending authority made available to the SBA by congressional appropriation. Cumulative Results of Operations reflects the net results of SBA's operations over time. As of September 30, 2003 SBA's Net Position decreased by $1.43 billion due primarily to a decrease in Cumulative Results of Operations.

Statement of Net Cost

The Consolidated Statement of Net Cost shows, by major program, how much it cost SBA to provide its services for the fiscal year. Net cost is calculated by subtracting any earned revenues from gross costs.

FY 2003 costs were allocated between the SBA's three major programs: Champion Small Business Interests, Empowering Entrepreneurs, and Disaster Assistance Programs. A small residual amount was attributable to a "Costs Not Assigned to Programs" category, that included the costs of the SBA's Inspector General and local initiatives funded by Congress in SBA's budget.

"In FY 2003, SBA's Net Cost of Operations was $3.17 billion, a 100% increase from the FY 2002 cost of $1.59 billion. The net increase of $1.58 billion is the result a $1.82 billion increase in Empowering Entrepreneurs costs, offset by a total decrease in costs of $.24 billion for Champion Small Business Interests, Disaster Assistance Programs, and Costs Not Assigned to Programs.

The $1.82 billion increase in net Empowering Entrepreneurs Program costs is due to an increase in both gross costs with the public and intragovernmental gross costs. The increase in intragovernmental gross costs is the result of an upward reestimate for loan subsidy in FY 2003.

The most significant portion of the decrease in costs is attributable to $.22 billion decrease in the net Costs of Disaster Assistance Programs, the result of a reduction in SBA's loss allowance expense and fewer program expenses. These reductions are attributable to a smaller credit receivable portfolio.

The following tables provide a comparison of costs in dollars and percentages for the two most recent fiscal years:

COST IN DOLLARS (IN MILLIONS)

	2003			2002 Restated		
	Intragovt.	Public	Total	Intragovt.	Public	Total
Champion Small Business Interests	$3.0	$11.0	$14.0	$3.5	$14.7	$18.2
Empowering Entrepreneurs	$25.2	$2,654.5	$2,679.7	-$62.7	$924.8	$862.1
Disaster	$252.7	$172.4	$425.1	$248.1	$396.4	$644.5
Not Assigned	n/a	n/a	$52.9	n/a	n/a	$63.9
Total	$280.9	$2,837.9	$3,171.7	$188.9	$1,335.9	$1,588.7

COST AS PERCENTAGES (IN MILLIONS)

	2003			2002 Restated		
	Intragovt.	Public	Total	Intragovt.	Public	Total
Champion Small Business Interests			0.4%			1.1%
Empowering Entrepreneurs			84.5%			54.3%
Disaster			13.4%			40.6%
Not Assigned			1.7%			4.0%
Total			100.0%			100%

Statement of Changes in Net Position

The Consolidated Statement of Changes in Net Position shows SBA's beginning and ending net position by two major components, Cumulative Results of Operations and Unexpended Appropriations, both of which are also shown on the Balance Sheet. The Statement of Changes in Net Position provides detail support of the major categories of items that caused the net position to change during the year. For FY 2003, the most significant change in net position resulted from the increase in cost of operations, see Statement of Net Cost discussion.

Budgetary Resources

The Combined Statement of Budgetary Resources provides information about the funding and availability of budgetary resources and the status at the end of the reporting period. It is the only financial statement from which data is derived exclusively from budgetary accounts in the general ledger.
Data on the Combined Statement of Budgetary Resources is consistent with budget execution information on the SF 133 Report on Budget Execution Budgetary Resources, with one exception. A line item, Offsetting Receipts, has been added to the Combined Statement of Budgetary Resources. Offsetting receipts are used to offset budgetary authority and outlays at the agency level and are presented in this statement to reconcile outlay information in the Budget of the United States Government.

Total budgetary resources for SBA were $7.51 billion, a decrease of $4.39 billion from FY 2002. The majority of SBA's funding was derived from the previous year's unobligated balance and offsetting collections. Appropriations, borrowing authority, recoveries from prior year obligations, and non-available funding rounded out the balance of total budgetary resources.

Funding is further pro-rated between budgetary financing (38%) and non-budgetary financing (62%). The FY 2003 appropriation of $1.98 billion provided the most significant portion of the $2.82 billion of budgetary financing. The largest source of funding for the $4.68 billion non-budgetary financing was from FY2002 unobligated balances of $6.05 billion.

The following tables show a comparison of the two most recent fiscal years of total budgetary resources available for use and the status of resources:

Budgetary Resources

(DOLLARS IN BILLIONS)

	Budget Authority	Unobligated Balance (1 Oct)	Spending Authority from Offsetting Collections	Recoveries of Prior Year Obligations	Permanently not Available	Total Budgetary Resources
2003	$3.14	$6.76	$3.43	$0.21	($6.03)	$7.51
2002 Restated	$3.15	$7.46	$3.19	$0.29	($2.20)	$11.89

Status of Budgeary Resources

(DOLLARS IN BILLIONS)

	Obligations Incurred	Unobligated Balances Available	Unobligated Balances Not Available	Total Status of Budgetary Resources
2003	$5.32	$1.52	$0.67	$7.51
2002 Restated	$5.13	$3.05	$3.71	$11.89

Statement of Financing

The Consolidated Statement of Financing shows the relationship between SBA's net obligations drawn from budgetary accounting and net cost of operations drawn from proprietary accounting by identifying key differences between the two amounts. The statement shows total resources used within the reporting period and adjustments to these resources based upon their usage to finance net obligations or net cost.

Budgetary resources obligated in FY 2003 were $5.32 billion, a 4% increase from FY 2002 obligations of $5.13 billion. Spending authority from offsetting collections and recoveries of $3.64 billion was an increase of 5% from the previous year's amount of $3.47 billion. Both of these categories (less offsetting receipts), which sum to the net obligations, can be tied to amounts in the Combined Statement of Budgetary Resources. Net obligation, transfers in (out), and resources used to finance items not part of the net cost of operations result in the Total Resources Used to Finance the Net Cost of Operations.

Adjustments to the Total Resources Used to Finance the Net Cost of Operations created the Total Resources Used to Finance Net Cost of Operations of $1.8 billion, an increase of 377% from the previous year's amount of $.38 billion. The major adjustment item was in the Components of the Net Cost of Operations that will not Require or Generate Resources in the Current Period, i.e., 'Upward/Downward re-estimates of Credit Subsidy Expense'. Net Cost of Operations is also shown on the Statement of Net Cost and the Statement of Net Position.

Consolidated Balance Sheet

Consolidated Balance Sheet as of September 30, 2003 and 2002 (DOLLARS IN THOUSANDS)	2003	Restated 2002
ASSETS		
Intragovernmental Assets		
Fund Balances with Treasury (Note 2)	**$2,798,677**	$7,492,741
Accounts Receivable (Note 5)	**12,650**	530
Total Intragovernmental	**2,811,327**	7,493,271
Cash (Note 3)	**5,331**	3,458
Accounts Receivable (Note 5)	**35,472**	76,973
Credit Program Receivables and Related Foreclosed Property, Net (Note 6)	**4,300,333**	4,596,954
General Property and Equipment, Net (Note 7)	**8,522**	6,828
Advances and Other Assets (Note 8)		23,287
Total Assets - Public	**4,349,658**	4,707,500
Total Assets	**$7,160,985**	$12,200,771
LIABILITIES		
Intragovernmental Liabilities		
Accounts Payable	**$13,737**	$24,885
Debt (Note 10)	**6,706,379**	11,141,384
Other (Note 12)	**840,396**	1,219,513
Total Intragovernmental	**7,560,512**	12,385,782
OTHER LIABILITIES - PUBLIC		
Accounts Payable	**49,648**	127,807
Liabilities for Loan Guarantees (Note 6)	**2,548,963**	1,241,593
FECA Actuarial Liability (Note 11)	**31,822**	31,487
Other (Note 12)	**140,288**	157,433
Total Other Liabilities - Public	**2,770,721**	1,558,320
Total Liabilities	**$10,331,233**	$13,944,102
NET POSITION		
Unexpended Appropriations	**$847,474**	$954,635
Cumulative Results of Operations	**(4,017,722)**	(2,697,962)
Total Net Position	**$(3,170,248)**	$(1,743,327)
Total Liabilities and Net Position	**$7,160,985**	$12,200,775

The accompanying notes are an integral part of these statements.

Consolidated Statement of Net Cost

Consolidated Statement of Net Cost
for the periods ended September 30, 2003 and 2002
(DOLLARS IN THOUSANDS)

Programs	2003	Restated 2002
Champion Small Business Interests		
Intragovernmental Gross Costs	**$2,951**	$3,453
Less: Intragovernmental Earned Revenue	**0**	0
Intragovernmental - Net Costs	**$2,951**	$3,453
Gross Costs with the Public	**$10,984**	$14,732
Less: Earned Revenue from the Public	**0**	0
Net Costs with the Public	**$10,984**	$14,732
Net Cost of Champion Small Business Interests	**$13,935**	$18,185
Empowering Entrepreneurs		
Intragovernmental Gross Costs	**$78,487**	$(8,004)
Less: Intragovernmental Earned Revenue	**53,335**	32,148
Intragovernmental - Net Costs	**$25,152**	$(40,152)
Gross Costs with the Public	**$3,153,943**	$1,113,346
Less: Earned Revenue from the Public	**499,401**	188,576
Net Costs with the Public	**$2,654,542**	$924,770
Net Cost of Empowering Entrepreneurs	**$2,679,694**	$884,618
Disaster Assistance Programs		
Intragovernmental Gross Costs	**$534,471**	$684,008
Less: Intragovernmental Earned Revenue	**281,724**	435,879
Intragovernmental - Net Costs	**$252,747**	$248,129
Gross Costs with the Public	**$396,915**	$654,635
Less: Earned Revenue from the Public	**224,490**	258,259
Net Costs with the Public	**$172,425**	$396,376
Net Cost of Disaster Assistance Programs	**$425,172**	$644,505
Cost not assigned to Programs	**$54,508**	$41,046
Less: Earned Revenue not attributed to Programs	**1,628**	(285)
Net Cost not assigned to Programs	**$52,880**	$41,331
Net Cost of Operations	**$3,171,681**	$1,588,639

(Note 13)
The accompanying notes are an integral part of these statements.

Consolidated Statement of Changes in Net Position

Consolidated Statement of Changes in Net Position
for the periods ended September 30, 2003 and 2002

(DOLLARS IN THOUSANDS)

	2003			2002 Restated		
	Cumulative Results of Operations	Unexpended Appropriations	Total	Cumulative Results of Operations	Unexpended Appropriations	Total
Beginning Net Position - October 1				**$(879,335)**	**$1,043,274**	**$163,939**
Prior Period Adjustments				(825,455)	(6,843)	(832,298)
Beginning Net Position, as Adjusted	**$(2,697,964)**	**$954,633**	**$(1,743,331)**	**(1,704,790)**	**1,036,431**	**(668,359)**
Budgetary Financing Sources						
Appropriations Received		1,982,908	1,982,908		1,013,208	1,013,208
Appropriations Transferred - in/out (+/-)		(9,000)	(9,000)			
Rescissions		(29,369)	(29,369)		(5,984)	(5,984)
Adjustment - Cancelled Authority		(5,978)	(5,978)		(24,154)	(24,154)
Other Adjustments		(30,581)	(30,581)	271	(205)	66
Appropriations Used	2,015,139	(2,015,139)		1,064,665	(1,064,665)	
Donations of Cash and Cash Equivalents	207		207	133		133
Transfers - in/out Without Reimbursement (+/-)						
Other Financing Sources						
Transfers - in/out Without Reimbursement (+/-)	(175,608)		(175,608)	(263,127)		(263,127)
Imputed Financing from Costs Absorbed by Others	19,063		19,063	17,420		17,420
Other - Current Year Liquidating Equity Activity (+/-)	(6,878)		(6,878)	(223,895)		(223,895)
Total Financing Sources	**$1,851,923**	**$(107,159)**	**$1,744,764**	**$595,467**	**$(81,800)**	**$513,667**
Net Cost of Operations	**$3,171,681**		**$3,171,681**	**$1,588,639**		**$1,588,639**
Ending Net Position	**$(4,017,722)**	**$847,474**	**$(3,170,248)**	**$(2,697,962)**	**$954,631**	**$(1,743,331)**

(Note 14)
The accompanying notes are an integral part of these statements.

Combined Statement of Budgetary Resources

Combined Statement of Budgetary Resources
for the periods ended September 30, 2003 and 2002

(DOLLARS IN THOUSANDS)

	2003			2002 Restated		
	Budgetary	Non-Budgetary Financing	Total	Budgetary	Non-Budgetary Financing	Total
BUDGETARY RESOURCES						
Budget Authority						
Appropriations Received	$1,982,908		$1,982,908	$1,013,208		$1,013,208
Borrowing Authority		1,158,196	1,158,196		2,168,244	2,168,244
Net Transfers (+/-)				(29,545)		(29,545)
Other						
Unobligated Balance						
Brought Forward October 1	711,921	6,049,860	6,761,781	1,306,037	6,154,082	7,460,119
Net Transfers (+/-)	(9,000)		(9,000)			
Spending Authority from Offsetting Collections						
Earned	487,232	2,963,617	3,450,849	449,048	2,534,651	2,983,699
Change in Unfilled Customer Orders	(8,898)	(12,930)	(21,828)	61,248	140,913	202,161
Recoveries of Prior Year Obligations	125,914	85,615	211,529	81,373	205,855	287,228
Permanently Not Available	(461,412)	(5,567,309)	(6,028,721)	(691,458)	(1,502,478)	(2,193,936)
Total Budgetary Resources	**$2,828,665**	**$4,677,049**	**$7,505,714**	**$2,189,911**	**$9,701,267**	**$11,891,178**
STATUS OF BUDGETARY RESOURCES						
Obligations Incurred	$2,412,968	$2,907,847	$5,320,815	$1,477,992	$3,651,407	$5,129,399
Unobligated Balances Available						
Apportioned - Currently Available	287,327	1,236,696	1,524,023	335,356	2,714,670	3,050,026
Exempt from Apportionment	357		357	104		104
Unobligated Balances Not Available	128,013	532,506	660,519	376,459	3,335,190	3,711,649
Total Status of Budgetary Resources	**$2,828,665**	**$4,677,049**	**$7,505,714**	**$2,189,911**	**$9,701,267**	**$11,891,178**

Combined Statement of Budgetary Resources
for the periods ended September 30, 2003 and 2002

(DOLLARS IN THOUSANDS)

	2003			2002 Restated		
	Budgetary	Non-Budgetary Financing	Total	Budgetary	Non-Budgetary Financing	Total
Relationship Of Obligations To Outlays						
Obligated Balance, End of Period						
Accounts Receivable	(3,264)	(34,862)	(38,126)	(16,757)	(56,021)	(72,778)
Unfilled Customer Orders from Federal Sources	(233)	(127,983)	(128,216)		(140,913)	(140,913)
Undelivered Orders	382,886	261,053	643,939	425,284	242,667	667,951
Accounts Payable	94,549	41,623	136,172	115,341	161,358	276,699
Total Obligated Balance, End of Period	**473,938**	**139,831**	**613,769**	**523,868**	**207,091**	**730,959**
Outlays						
Disbursements	2,350,241	2,923,581	5,273,822	1,455,526	4,204,614	5,660,140
Collections	(491,596)	(2,984,774)	(3,476,370)	(559,900)	(3,014,707)	(3,574,607)
Subtotal	**1,858,645**	**(61,193)**	**1,797,452**	**895,626**	**1,189,907**	**2,085,533**
Less: Offsetting Receipts		299,819	299,819		403,861	403,861
Net Outlays	**$1,858,645**	**$(361,012)**	**$1,497,633**	**$895,626**	**$786,046**	**$1,681,672**

(Note 15)
The accompanying notes are an integral part of these statements.

Consolidated Statement of Financing

Consolidated Statement of Financing
for the periods ended September 30, 2003 and 2002

(DOLLARS IN THOUSANDS)

	2003	Restated 2002
Resources Used to Finance Activities		
Budgetary Resources Obligated		
Obligations Incurred	**$5,320,815**	$5,129,399
Less: Spending Authority from Offsetting Collections and Recoveries	**3,640,550**	3,473,088
Obligations Net of Offsetting Collections and Recoveries	**1,680,265**	1,656,311
Less: Offsetting Receipts	**299,819**	403,861
Net Obligations	**$1,380,446**	$1,252,450
Other Resources		
Transfers In (Out)	**(175,608)**	(263,127)
Imputed Financing	**19,063**	17,420
Other Financing Sources	**(6,878)**	(223,895)
Net Other Resources Used to Finance Activities	**$(163,423)**	$(469,602)
Total Resources Used to Finance Activities	**$1,217,023**	$782,848
Resources Used to Finance Items not Part of the Net Cost of Operations		
Change in Undelivered Orders	**12,025**	326,467
Budgetary Offsetting Collections and Receipts that Do Not Affect Net Cost of Operations	**2,963,617**	2,534,651
Resources that Finance the Acquisition of Assets or Liquidation of Liabilities	**(2,392,133)**	(3,259,702)
Adjustments to Net Obligated Resources That Do Not Affect Net Cost of Operations	**1,320**	(6,255)
Total Resources Used to Finance Items Not Part of the Net Cost of Operations	**$584,829**	$(404,839)
Total Resources Used to Finance the Net Cost of Operations	**$1,801,852**	$378,009
Components of the Net Cost of Operations that will not Require or Generate Resources in the Current Period		
Components Requiring or Generating Resources in Future Periods		
Change in Annual Leave Liability	**$650**	$754
Upward/ Downward reestimates of Credit Subsidy Expense	**1,319,587**	986,926
Change in Revenue Receivable from Public	**7,963**	50,632
Change in Due to Treasury - Liquidating Funds that is not an obligation	**6,880**	223,897
Provision for Losses on Estimated Guarantees	**10,092**	(248,098)
Unfunded Employee Benefits	**671**	(661)
Total Components of the Net Cost of Operations that will not Require or GenerateResources in the Current Period	**$1,345,843**	$1,013,450
Components Not Requiring or Generating Resources		
Depreciation or Amortization	**3,018**	2,521
Bad Debt Expense - Noncredit Reform	**20,968**	194,659
Total Components of Net Cost that will Not Require or Generate Resources	**23,986**	197,180
Total Components of Net Cost of Operations Not Requiring or Generating Resources in the Current Period	**$1,369,829**	$1,210,630
Net Cost of Operations	**$3,171,681**	$1,588,639

(Note 16)
The accompanying notes are an integral part of these statements.

NOTES TO FINANCIAL STATEMENTS

Notes to Financial Statements
for the periods ended September 30, 2003 and 2002

NOTE 1. Significant Accounting Policies

A. Basis of Accounting and Presentation

These financial statements have been prepared from the accounting records of the U.S. Small Business Administration (SBA) maintained in accordance with generally accepted accounting principles (GAAP) of the United States as delineated by the Federal Accounting Standards Advisory Board (FASAB).

The statements reflect transactions recorded on both a proprietary accrual accounting basis, in accordance with GAAP, and a budgetary obligation basis, in accordance with concepts and guidance provided by the Office of Management and Budget (OMB) in Circular A-11, "Preparation, Submission, and Execution of the Budget". Under the accrual method, revenues are recognized when earned and expenses are recognized when liabilities are incurred, without regard to receipt or payment of cash. Budgetary accounting recognizes legal obligation of funds often in advance of the proprietary accrual, and facilitates compliance with legal constraints and controls over the use of Federal funds.

Management has, in accordance with GAAP, made assumptions and estimates which were used in the preparation of the financial statements. These estimates and assumptions have an effect on reported assets and liabilities, contingent liabilities as disclosed, and the amount of revenues and expenses reported for the period.

B. Reporting Entity

The SBA was created as an independent Federal Agency by the Small Business Act of 1953. Its mission is to maintain and strengthen the Nation's economy by aiding, counseling, assisting, and protecting, the interests of small business, and to help businesses and families recover from disasters.

The Business Loan, 504 Development Company and SBIC Investment Company programs are the SBA's major credit programs to assist small business. The SBA's non-credit programs providing small business assistance include Surety Bond Guarantees (SBG), Business Development for minority firms, Government Contracting assistance and Entrepreneurial Development assistance to counsel and train small business people. In addition, the SBA Advocacy Program promotes the interests of small business in government legislative and regulatory forums. The SBA's Disaster Loan program provides assistance to victims of physical disasters such as earthquakes, floods, and hurricanes by extending direct loans to individuals and businesses.

The SBA operates through the execution of a congressionally approved budget that funds its programs. The SBA's budget consists of annual, multi-year and no-year appropriations which fund salaries and expenses and various program activities.

Under the aegis of the Federal Credit Reform Act of 1990 (FCRA), as amended, the SBA utilizes Program and Financing Accounts to record events for its business direct and guaranteed loans and disaster loans, as well as Liquidating Accounts for its Pollution Control Equipment Guarantees and Pre-FY 1992 business and disaster loans. A Revolving fund is used to record Surety Bond Guarantees accounting events and Administrative funds are used to account for Salaries and Expenses of the Agency and its Inspector General. Finally, a trust fund, funded by donations made by non-Federal entities, is used to record accounting events for business assistance.

C. Budgets and Budgetary Accounting for Loan Programs

The SBA's loan disbursements are financed by a combination of two sources: one for the long term cost of the loan and another for the remaining non-subsidized portion of the loan. Congress provides one-year, multi-year, and no-year appropriations to cover the estimated long term costs of SBA loans. The long term costs are defined as the net present value of the estimated cash outflows associated with the loans less the estimated cash inflows. The portion of each loan disbursement that does not represent long term cost is financed under a permanent indefinite authority to borrow funds from the U.S. Department of the Treasury (Treasury). Congress also annually adopts an appropriation bill limiting the dollar amount of obligations that can be made for direct loans and loan guarantees.

A permanent indefinite appropriation is available to finance the costs of subsidy re-estimates that occur after the year in which a loan is disbursed. Modification of loans or loan guarantees require that budget authority for the additional cost be appropriated, if not available from existing appropriations or other budgetary resources.

D. Fund Balances with Treasury and Cash

Fund Balances with Treasury and cash consist primarily of appropriated, revolving and trust funds, which are available to make expenditures and pay liabilities. Cash receipts and disbursements are processed by the Treasury. Amounts are also included in Fund Balances which are unavailable for obligation because they relate to expired authority. (See Notes 2 & 3)

E. Accounts Receivable

Accounts Receivable - Intergovernmental are reimbursements due from other Federal agencies and funds. The SBA records intrafund receivables and payables between program and financing funds for its subsidy reestimates.

Accounts Receivable which are not intragovernmental primarily represent amounts due from participating financial institutions for guarantee fees and advances from asset sale purchasers. The balance in the Salaries and Expenses fund represents receivables due from Agency employees or vendors for net credits from various transactions. (See Note 5.)

The SBA has determined that uncollectible or unrecoverable accounts are not significant and does not provide an allowance. The historic immateriality of losses is due to stringent collection policy and the ability to offset against the lender's share of collections, payments to employees, or payments to vendors.

F. Credit Program Receivables and Related Foreclosed Property

Reporting requirements for direct loan obligations made after fiscal year 1991 are governed by the FCRA. The FCRA requires that the present value of the subsidy costs (present value of the estimated cash outflows over the life of the loans minus the present value of the estimated cash inflows, discounted at the interest rate of marketable Treasury securities with a similar maturity term) associated with direct loans be recognized as a cost in the year that the loan is obligated. Direct loans are reported net of an allowance for subsidy at the present value.

Loans that were obligated prior to the FCRA are recorded at book value with an allowance for uncollectible amounts.

The SBA advances payments semiannually to the Federal Financing Bank for loans guaranteed under Section 503 of the Small Business Act. The advances are liquidated by receipt of the next installment payments from state and local development companies. To the extent that those installments may not repay advances, balances remain collectible from the development companies.

Advances are also made to honor the SBA's timely payment requirement of principal and interest due for debentures in the SBA's Section 503, Section 504 and SBIC programs.

G. General Property and Equipment

Equipment is capitalized at full cost, if the initial unit acquisition full cost is $50,000 or more and service life is at least five years. Equipment with an acquisition cost of less than $50,000 or less than five years of life is expensed when purchased. Equipment is depreciated using the straight-line method over five years. Computer related equipment is capitalized at cost, if the initial unit acquisition cost is $50,000 or more and has a service life of at least three years. Computer related equipment and software with an acquisition cost of less than $50,000 or less than three years of life is expensed when purchased. Computer related equipment and software is depreciated using the straight-line method over three years.

Software for internal use, whether internally developed, contractor developed, or commercial off-the-shelf (COTS), is capitalized at cost provided that the initial unit acquisition cost is $250,000 or more and has a service life of at least two years. For internally developed software, the capitalizable costs are the direct and indirect costs incurred after the SBA has completed all planning, designing, coding and testing activities that are necessary to establish that the software can meet design specifications up to the point of final acceptance. Software for internal use is depreciated using the straight-line method over its useful life. The costs of enhancements are capitalized when it is more likely than not that the enhancements will result in significant additional capabilities. Costs that do not meet the capitalization criteria are expensed when incurred.

H. Debt

Borrowings payable to the Treasury result from loans provided by the Treasury to fund a portion of the Agency's credit reform financing accounts activity. The financing accounts are required to make periodic principal payments to Treasury based on the collections of loans receivable.

Borrowings payable to the Federal Financing Bank (FFB) result from a sale of loans to the FFB of loans from the Business Liquidating Account. As the FFB collects the principal of these loans the SBA's liability to FFB is reduced as well as an offsetting Loan Receivable. (See Note 10).

I. Liability for Loan Guarantees

There are two components to the Agency's liability for guaranteed loans: liabilities for losses on pre-1992 loans, and liabilities on post-1991 loans made under the Federal Credit Reform (FCR) legislation. For pre-1992 guarantees, the amount is an estimate of losses on guarantees outstanding based on historical experience. For post-1991 loans, the liability is based on the present value of future cash flows related to the guarantees. (See Note 6-L).

J. **Contingencies**

The SBA is a party in various administrative proceedings, legal actions, environmental suits and claims brought against it. In the opinion of the SBA management and legal counsel, the ultimate resolution of these proceedings, actions, suits and claims will not materially affect the financial position or results of the SBA operations. The likelihood of loss to the SBA ranges from remote to probable for these litigation matters. (See Note 12).

K. **Leave**

A liability for annual leave is accrued as it is earned and reduced as leave is taken. Each year, the balance in the accrued annual leave is adjusted to reflect current pay rates. To the extent current or prior year appropriations are not available to fund annual leave earned but not taken, funding will be obtained from future appropriations.

Sick leave and other types of non-vested leave are expensed as taken.

L. **Employee Health and Life Insurance Benefits**

SBA employees are eligible to participate in contributory Federal Employees Health Benefit program (FEHB) and the Federal Employees Group Life Insurance program (FEGLI). The SBA matches a portion of the employee contributions to each program. These contributions are recognized as current operating expenses.

M. **Employee Pension Benefits**

SBA employees participate in either the Civil Service Retirement System (CSRS) or the Federal Employees' Retirement System (FERS). Most employees hired after December 31, 1983 are covered by FERS. These systems provide benefits upon retirement and may also provide benefits for death, disability, or other termination of employment before retirement. They may also include benefits to survivors and dependents, and they may contain early retirement or other special features. The CSRS and FERS retirement funds are administered by the Office of Personnel Management (OPM).

For CSRS, SBA contributes 7.0 percent of the employee gross earnings in addition to the 7.0 percent withheld from the employee. For FERS, SBA withholds .8 percent of gross earnings, and matches the withholding with a 10.7 percent employer contribution. SBA contributions to the CSRS and FERS are recognized as current operating expenses. SBA's contribution to CSRS was $6.5 million and $7.8 million in FY 2003 and FY 2002 respectively, and $16.1 million and 14.7 million FERS in these years. The imputed cost for the two programs was $7.4 million for FY 2003 and $6.4 million for FY 2002. FERS participants are also covered under the Federal Insurance Contribution Act (FICA) and are subject to FICA withholdings. The SBA makes matching contributions for FICA, recognized as operating expenses.

Federal employee benefits also include the Thrift Savings Plan (TSP), CSRS participants may contribute up to 8% of their gross pay (9% beginning October, 2003) to the TSP, but there is no Agency matching contribution. FERS participants may contribute up to 13% (14% beginning October, 2003) of their gross pay to the TSP. For FERS, SBA contributes 1% of basic pay and matches any employee contributions dollar for dollar for the first 3% of pay, and 50 cents on the dollar for the next 2% of pay. The SBA contributions to the TSP are recognized as current operating expenses. The maximum limit that either FERS or CSRS employees may contribute to the TSP is $12,000 ($13,000 beginning January, 2004).

The SBA recognizes the full cost of providing future CSRS and FERS pension benefits at the time the employees' services are rendered. The cost of pension benefits represents the actuarial present value of future benefits attributed to services rendered by covered employees during the accounting period, net of the amounts contributed by these employees. In addition, the OPM finances the excess of total pension expense over the amount contributed by the Agency and its employees. The SBA recognized this as non-exchange revenue and an imputed source. The SBA does not report in its financial statements FERS or CSRS assets, accumulated plan benefits or unfunded liabilities, if any applicable to its employees.

N. Other Retirement Benefits

SBA employees eligible to participate in the FEHB and the FEGLI may continue to participate in these programs after their retirement. SBA recognizes a current operating expense for the future cost of these and other retirement benefits (ORB) at the time the employee's services are rendered. This ORB expense must be financed by the OPM, and is offset by the SBA through recognition of an imputed financing source. Using cost factors supplied by the OPM, the SBA recorded ORB expense and imputed financing sources of $11.7 million for FY 2003 and $11.1 million for FY 2002.

O. Revenues and Other Financing Sources

The SBA recognizes as revenues and other financing sources appropriations used, earned revenue, donations, imputed financing sources, and non-expenditure transfers.

The SBA receives the majority of the funding needed to support its operations through congressional appropriations. The Agency receives one year, multi-year and no year appropriations that may be used, within statutory limits, for operating expenditures. A financing source, appropriations are considered used when good or services financed by an appropriation are provided, regardless of when paid. This is reported in the Consolidated Statement of Changes in Net Position.

Earned revenue results from exchange transactions that benefit both parties. The SBA has earned revenues such as loan guarantee fees, interest on its loan portfolios, and interest on fund balances. These revenues are presented on the Consolidated Statement of Net Cost as reductions to operating cost.

Donations are treated as revenues and reported in the Consolidated Statement of Changes in Net Position.

Imputed financing sources are operating costs of the SBA which are paid for through funds appropriated to other Federal entities. These include items such as employee pension benefits and post-employment benefits for former employees. The imputed financing source is reported in the Consolidated Statement of Changes in Net Position while the associated cost is reflected in the Consolidated Statement of Net Cost.

Non-expenditure transfers of appropriated amounts or of assets without reimbursement included items such as transfers to Treasury of downward subsidy reestimates and unobligated balances from liquidating accounts. These transfers are included in the Consolidated Statement of changes in Net Position.

NOTE 2. Fund Balances with Treasury

(DOLLARS IN THOUSANDS)

Fund Balances	FY 2003	FY 2002
Entity		
Trust Fund	$440	$278
Liquidating Funds	245,606	492,845
Financing Funds	1,909,033	6,256,953
Revolving Fund	22,978	26,706
Appropriated Funds	620,620	715,959
Total Fund Balances	**$2,798,677**	**$7,492,741**
Status of Fund Balances with Treasury		
Unobligated Balance		
Available	$1,524,389	$3,050,133
Unavailable	660,519	3,711,649
Obligated Balance Not Yet Disbursed	613,769	730,959
Total	**$2,798,677**	**$7,492,741**

NOTE 3. Cash

Cash held outside the U.S. Treasury consists of undeposited funds under the control of the SBA at field offices or lock boxes.

(Dollars in Thousands)

Cash	FY 2003 Entity Assets	FY 2002 Entity Assets
At Field Offices	$4,975	$3,391
Lock boxes	356	67
	$5,331	**$3,458**

NOTE 4. Master Reserve Fund

The Small Business Secondary Market Improvements Act of 1984, P.L. 98-352 (Improvement Act) provided statutory authority for the 7(a) secondary market, for the pooling of 7(a) loans, for the central registration of secondary market loans and for improved disclosure of 7(a) secondary market loans. The Improvement Act also provided for SBA's regulation of brokers and dealers operating in the 7(a) secondary market and for reporting to Congress on secondary market results. The 7(a) secondary market has approximately $13 billion of currently outstanding investments held by 7(a) secondary holders.

It is the intent of Congress in the Improvement Act that the 7(a) secondary market pooling program has no cost to the Federal taxpayer. The Master Reserve Fund (MRF), maintained by the SBA's fiscal agent as part of its administration of the 7(a) secondary market program, is the device created to fulfill this intent. The MRF also provides for the pooling of loans having terms that vary within a range prescribed by the SBA while the secondary investors have a fixed term for their investment that is the term of the longest loan in the pool. The MRF is funded by the timing of cashflows in the 7(a) secondary market program, including the principal portion of the borrower's first payment for pooled loans and the float on borrower payments prior to payment to the secondary holders. It used to fund the SBA's guarantee of the timely payment of principal and interest owed to the 7(a) secondary market holders and to pay expenses of the MRF trustee and investment advisor.

The composition of the MRF at September 30, 2003 and September 30, 2002 is shown in the following table. A reconciliation of the change in MRF assets from September 30, 2002 and September 30, 2003 is also shown.

Master Reserve Fund (DOLLARS IN THOUSANDS)		
	9/30/03	**9/30/02**
Receivables		
Securities – Repurchase Agreements	$231,000	$218,000
Net Interest	12,672	13,183
Interest Sold/Matured		11
Total Receivables	**$243,672**	**$231,194**
Payables		
Government Bonds		
Treasury Bonds	$123,719	$166,835
Treasury Notes	709,935	644,537
Total Government Bonds	**$833,654**	**$811,372**
Cash Equivalents – Money Market Funds	$26,848	$27,444
Short Term Investments – Treasury Bills	$155,616	$143,384
Net Assets	**$1,259,790**	**$1,213,383**
Master Reserve Fund	**$1,259,790**	**$1,213,383**

Reconciliation of MRF Assets	
Beginning Net Assets – 9/30/02	$1,213,383
Receipts	
Regular Loan Payments	1,219,237
Prepayments	961,202
Defaults from SBA or the Lender	564,800
Other Receipts1	(9,850)
Earned Income	55,246
Net Realized Gain (Loss)	(1,028)
Total Receipts	**2,789,607**
Disbursements	
Regular Payments to Investors	1,215,445
Prepayments	961,202
Defaults	564,800
Expenses	1,753
Total Disbursements	**$2,743,200**
Ending Net Assets – 9/30/03	**$1,259,790**

The MRF is invested approximately 20 percent in short term (6 month) Treasury securities and 80 percent in long term Treasuries (5 years). The earnings on these investments are used to pay the cost of making the timely payment to 7(a) secondary market investors. The central issue is whether the earnings of the MRF are adequate to fund timely payment during the future liquidation of the current secondary market portfolio. Various factors influence MRF adequacy including the earning rate on MRF short and long term investments, the interest rate paid to investors, the "spread" of maturities in the loan pools, the occurrence of prepayments and delinquency, float on monthly payments and prepayments, holdback of the principal portion of the first payment, and the pattern of liquidation of loans in 7(a) secondary market pools.

The SBA is liable to secondary market investors in the future if the MRF could not fund the liquidation of 7(a) secondary market pools. With this in mind, the SBA agreed with the Office of Management and Budget in November 2002 to include the MRF under the requirements of the Federal Credit Reform Act of 1990 as the Secondary Market Guarantee (SMG) program beginning with the FY 2005 budget. Also, the SBA agreed to reestimate the cost of the SMG program annually beginning with FY 2002. The SBA will account for the SMG program within its Business Loan Program Account and its Business Guarantee Financing Account.

A thorough analysis of MRF adequacy was conducted by the Agency during FY 2003. The status of the MRF was evaluated at the end of fiscal years 2002 and 2003. In addition, the performance of 7(a) loans from SBA's 7(a) program modeling experience was applied to these fiscal year results in order to project the liquidation of the secondary market portfolio outstanding as of September 30, 2003. The conclusion of this analysis was that the MRF will not be sufficient after 2017 to liquidate the secondary market portfolio. Additional funding of $ 72 million for FY 2002 and $19 million for FY 2003 would be needed to fully liquidate the September 30, 2003 portfolio.

The SBA has restated its FY 2002 financial statements to reflect the $72 million shortfall as a subsidy requirement; the Agency's FY 2003 financial statements reflect an additional $19 million SMG subsidy increment. The SBA's FY 2002 financial statements originally included footnote disclosure for the SMG with a potential deficit in the range of zero to $18.3 million. This amount was not included the SBA's financial statements as a contingent liability because the likelihood of the liability was deemed to be remote. The aforementioned extensive analysis performed on the MRF supports this change in accounting treatment during FY 2003.

The SBA, nonetheless, expects to make changes to the 7(a) secondary market program which will provide additional MRF income resulting in a subsidy rate of zero for the SMG. A zero subsidy rate meets the intent of Congress that the program should not create an additional cost or liability to the government and that the SBA's secondary market pooling program should have a zero budgetary impact.

NOTE 5. Accounts Receivable

Accounts receivable are displayed by type. Additional information about the types of receivables is contained in Note 1E.

Cash adjustments are Funds with Treasury transactions that Treasury has not applied as of the Balance Sheet date or Treasury transactions that SBA has not recorded due to timing differences.

By Type

	FY 2003		FY 2002 - Restated	
	Intra-governmental	Public	Intra-governmental	Public
Subsidy Receivable from Program Fund to Financing Fund	$3,695,058	$	$2,375,471	$
Interest Receivable From Treasury	12,643			
Other Intrafund Receivables	25,880		72,610	
Overpayment to Secondary		401		578
Guarantee Fees Receivable		26,702		49,003
Examination Fees - SBIC		76		76
Administrative Receivables		81		616
Refunds		4,288		4,140
Revenue Receivable		1,587		1,001
Receivable due from Banks		2,288		724
Cash Adjustments				20,698
Receivable due from Purchasers				
- Asset Sales		49		137
Reimbursables	1,688		530	
Sub-Total Before Eliminations	**$3,735,269**	**$35,472**	**$2,448,611**	**$76,973**
Eliminations - Intrafund Receivables	$(25,880)		$(72,610)	
Eliminations - Subsidy	(3,695,058)		(2,375,471)	
Eliminations - Reimbursables	(1,681)			
Balance Sheet Total	**$12,650**	**$35,472**	**$530**	**$76,973**

NOTE 6. Credit Program Receivables and Related Foreclosed Property

A. The SBA operates the following loan and loan guarantee programs:

(1) Business, Direct

(2) Disaster, Direct

(3) Business, Guarantee

(4) Pollution Control, Guarantee

Direct loan obligations and defaulted guarantee commitments made prior to 1992 are reported net of an allowance for estimated uncollectible loans or estimated losses. Loss allowances represent estimates of what the SBA does not expect to recover on its loans receivable obligated prior to FY 1992. These allowances are based upon historical experience, current market conditions and an analysis of individual assets. They are unfunded and merely attempt to reflect the anticipated uncollectible loans receivable. The SBA establishes a 100% allowance for pre-credit reforms that are past due more than 180 days.

"Direct loan obligations or loan guarantee commitments made after FY 1991, and the resulting direct loans or loan guarantees, are governed by the Federal Credit Reform Act. The Act provides that the present value of the subsidy costs (i.e., interest rate differentials, interest subsidies, estimated delinquencies and defaults, fee offsets, and other cash flows) associated with direct loans and loan guarantees be recognized as a cost in the year the loan or loan guarantee is disbursed.
"

An analysis of loans receivable, loan guarantees, liability for loan guarantees, and the nature and amounts of the subsidy and administrative costs associated with the loans and loan guarantees is provided in the following sections.

Interest receivable is comprised of accrued interest on accounts and loans receivable, and purchased interest related to defaulted guaranteed loans. Interest income is accrued at the contractual rate on the outstanding principal amount and is reduced by the amount of interest income accrued to non-performing loans (those in excess of 90 days delinquent). Purchased interest is carried at cost. A 100% allowance is established for all purchased interest on non-performing pre-credit reform loans.

Interest receivable is comprised of accrued interest on accounts and loans receivable, and purchased interest related to defaulted guaranteed loans. Interest income is accrued at the contractual rate on the outstanding principal amount and is reduced by the amount of interest income accrued to non-performing loans (those in excess of 90 days delinquent). Purchased interest is carried at cost. A 100% allowance is established for all purchased interest on non-performing pre-credit reform loans.

B. Direct Loans Obligated Prior to FY 1992:

(DOLLARS IN THOUSANDS)

FY 2003

Liquidating Loan Programs	Loans Receivable, Gross	Interest Receivable	Allowance for Loan Losses	Foreclosed Property	Value of Assets Related to Direct Loans
(1) Business	$48,817	$3,480	$(11,430)	$5,395	$46,289
(2) Disaster	53,146	337	(7,6090)	0	45,874
Total	**$101,963**	**$3,817**	**$(19,0120**	**$5,395**	**$92,163**

C. Direct Loans Obligated After FY1991:

(DOLLARS IN THOUSANDS)

FY 2003

Credit Reform Programs	Loans Receivable, Gross	Interest Receivable	Foreclosed Property	Allowance for Subsidy Cost (Present Value)	Net Present Value of Assets Related to Direct Loans
(1) Business	$129,158	$1,445	$0	$(13,323)	$117,280
(2) Disaster	2,938,237	33,247	1,346	(397,097)	2,575,733
Total	**$3,067,395**	**$34,692**	**$1,346**	**$(410,420)**	**$2,693,012**

D. Total Amount of Direct Loans Disbursed (Post-1991):

(DOLLARS IN THOUSANDS)

	FY 2003	FY 2002 - Restated
Credit Reform Programs		
(1) Business	$23,123	$25,205
(2) Disaster	686,149	1,225,255
Total	**$709,272**	**$1,250,460**

E. Subsidy Expense for Direct Loans by Program and Component Post-1991 Loans:

(DOLLARS IN THOUSANDS)

Subsidy Expense for New Direct Loans Disbursed FY 2003

Direct Loan Programs	Interest Differential	Defaults	Fees	Other	Total
(1) Business	$2,281	$74	$	$	$2,355
(2) Disaster	47,955	60,693	(6,711)	5,640	107,577
Total	**$50,236**	**$60,767**	**$(6,711)**	**$5,640**	**$109,932**

Subsidy Expense for New Direct Loans Disbursed FY 2002 - Restated

Direct Loan Programs	Interest Differential	Defaults	Fees	Other	Total
(1) Business	$2,005	$142	$	$	$2,147
(2) Disaster	109,905	110,274	(22,729)	16,790	214,240
Total	**$111,910**	**$110,416**	**$(22,729)**	**$16,790**	**$216,387**

Reestimates FY 2003

Direct Loan Programs	Technical Reestimates	Total Reestimates
(1) Business	$1,393	$1,393
(2) Disaster	135,310	135,310
Total	**$136,703**	**$136,703**

Reestimates FY 2002 - Restated

Loan Programs	Technical Reestimates	Total Reestimates
(1) Business	$1,139	$1,139
(2) Disaster	194,321	$194,321
Total	**$195,460**	**$195,460**

Modification Adjustment Transfer FY 2003

Loan Programs	Adjustment	Total
Disaster	$180,063	$180,063

Modification Adjustment Transfer FY 2002

Loan Programs	Adjustment	Total
Disaster	$151,575	$151,575

Total Direct Loan Subsidy Expenses

Loan Programs	FY 2003 Total	FY 2002 Restated Total
(1) Business	$3,748	$3,286
(2) Disaster	422,950	560,136
Total	**$426,698**	**$563,422**

F. Subsidy Rates for Direct Loans by Program and Component:

Budget Subsidy Rates for Direct Loans for the Current Year's Cohorts:

1. Direct Loans

FY 2003

Loan Programs	Interest Supplements	Defaults	Fees	Other	Total
(1) Business	12.84%	0.21%	0.00%	0.00%	13.05%
(2) Disaster	5.70%	8.53%	0.00%	-0.25%	13.98%
(3) Disaster-World Trade Center	10.64%	11.90%	-4.15%	4.81%	23.20%

G. Schedule for Reconciling Subsidy Cost Allowance Balances:

(DOLLARS IN THOUSANDS)

	(Post - 1991 Direct Business)		(Post - 1991 Direct Disaster)	
	FY 2003	FY 2002 - Restated	FY 2003	FY 2002 - Restated
Beginning balance of the subsidy cost allowance	$12,493	$23,748	$446,318	$(144,283)
Add: subsidy expense for				
Direct loans disbursed during the reporting years by component:				
Interest rate differential costs	2,281	2,005	47,955	109,905
Default costs (net of recoveries)	74	142	60,693	110,274
Fees and other collections			(6,711)	(22,729)
Other Subsidy Costs			5,640	16,790
Total of the above subsidy expense components	**2,355**	**2,147**	**107,577**	**214,240**
Adjustments:				
Loans written off	(331)	(121)	(143,195)	(108,981)
Subsidy allowance amortization	(3,662)	(14,420)	(152,180)	(395,195)
Prior Period Adjustment	1,075		3,267	686,216
Ending balance of the subsidy cost allowance	**11,930**	**11,354**	**261,787**	**251,997**
Add or subtract subsidy reestimatesby component:				
(a) Interest rate reestimate				
(b) Technical/ default reestimate	1,393	1,139	135,310	194,321
Total of the above reestimate components	**1,393**	**1,139**	**135,310**	**194,321**
Ending balance of the subsidy cost allowance	**$13,323**	**$12,493**	**$397,097**	**$446,318**

(Post - 1991 Guarantee Business)	FY 2003	FY 2002 - Restated
Beginning balance of the subsidy cost allowance	$526,444	$162,563
Adjustment related to the purchase of guaranteed loans	732,768	363,881
Other		
Ending balance of the subsidy cost allowance before reestimates	$1,259,212	$526,444

H. Defaulted Guaranteed Loans from Pre-1992 Guarantees:

(DOLLARS IN THOUSANDS)

FY 2003

Liquidating Loan Guarantee Programs	"Defaulted Guaranteed Loans Receivable, Gross"	"Interest Receivable"	"Allowance for Loan Losses"	"Foreclosed Property"	"Defaulted Guaranteed Loans Receivable, Net"
(1) Business	$258,111	$7,933	$(68,415)	$1,227	$198,856
(2) Pollution	48,503	433	(32,868)		$16,068
Total	**$306,614**	**$8,366**	**$(101,283)**	**$1,227**	**$214,924**

I. Defaulted Guaranteed Loans from Post-1991 Guarantees:

(DOLLARS IN THOUSANDS)

FY 2003

Credit Reform Loan Guarantee Program	"Defaulted Guaranteed Loans Receivable, Gross"	Advances	"Interest Receivable"	"Foreclosed Property"	Allowance for Subsidy Cost (Present Value)	"Net Present Value of Assets Related to Defaulted Guaranteed Loans Receivable"
(1) Business	$2,005,656	$516,190	$24,509	$13,091	$(1,259,212)	$1,300,234

J. Guaranteed Loans Outstanding:

(DOLLARS IN THOUSANDS)

	FY 2003		FY 2002	
Loan Programs	Outstanding Principal, Guaranteed Loans Receivable, Face Value	Amount of Outstanding Principal Guaranteed By SBA	Outstanding Principal, Guaranteed Loans Receivable, Face Value	Amount of Outstanding Principal Guaranteed By SBA
(1) Business	$53,641,745	$43,376,310	$50,089,639	$40,440,908
(2) Pollution	9,874	9,874	12,207	12,207
Total	**$53,651,619**	**$43,386,184**	**$50,101,846**	**$40,453,115**

K. Liability for Loan Guarantees:

(DOLLARS IN THOUSANDS)

FY 2003

Loan Programs	Liabilities for Loan Guarantees For Pre-1992 Guarantees	Liabilities for Loan Guarantees for Post-1991 Guarantees (Present Value)	Total Liabilities for Loan Guarantees
(1) Business	$5,464	$2,543,499	$2,548,963

FY 2002 - Restated

Loan Programs	Liabilities for Loan Guarantees For Pre-1992 Guarantees	Liabilities for Loan Guarantees for Post-1991 Guarantees (Present Value)	Total Liabilities for Loan Guarantees
(1) Business	$8,048	$1,233,403	$1,241,451
(2) Disaster	143		143
Total	**$8,191**	**$1,233,403**	**$1,241,594**

L. Subsidy Expense for Post-1991 Loan Guarantees:

(DOLLARS IN THOUSANDS)

Subsidy Expense for New Loan Guarantees

FY 2003

Loan Program	Defaults	Fees	Other	Total
Business	$398,266	($275,806)	($8,644)	$113,816

FY 2002

Loan Program	Defaults	Fees	Other	Total
Business	$483,037	$(339,382)	$(21,288)	$122,367

Reestimates FY 2003

Loan Program	Technical Reestimates	Total Reestimates
Business	$2,051,080	$2,051,080

Reestimates FY 2002 - Restated

Loan Programs	Technical Reestimates	Total Reestimates
Business	$535,453	$535,453

Modification Adjustment Transfer FY 2003

Loan Program	Adjustment	Total Reestimates
Business	$34,689	$34,689

Total Loan Guarantee Subsidy Expenses

Loan Program	FY 2003 Total	FY 2002 - Restated Total
Business	$2,199,585	$657,820

M. Subsidy Rates for Loan Guarantees by Program and Component:

Budget Subsidy Rates for Loan Guarantees for the Current Year's Cohorts:

FY 2003

Loan Programs	Defaults	Fees	Other	Total
Business				
7(a) and NAFTA	3.52%	-2.48%	0.00%	1.04%
7(a) Delta	4.07%	-2.49%	0.00%	1.58%
504 Debentures	3.02%	-5.61%	2.59%	0.00%
504 Delta	3.48%	-5.58%	2.98%	0.88%
SBIC Debentures	9.45%	-3.08%	-6.37%	0.00%
SBIC Participating Securities	6.58%	-3.08%	-3.50%	0.00%
SBIC New Markets	15.46%	0.00%	0.00%	15.46%
Microloan	1.82%	0.00%	6.60%	8.42%

N. Schedule for Reconciling Loan Guarantee Liability Balances:

(Post - 1991 Business Loan Guarantees)

(DOLLARS IN THOUSANDS)

	FY 2003	FY 2002 - Restated
Beginning balance of the loan guarantee liability	$1,233,403	$1,076,583
Add: subsidy expense for guarantee loans		
Default costs (net of recoveries)	398,266	483,037
Fees and other collections	(275,806)	(339,382)
Other Subsidy Costs	(8,644)	(21,288)
Total of the above subsidy expense components	**113,816**	**122,367**
Loans written off	(521,742)	(377,469)
Amortization of Subsidy	576,762	315,619
Restatement Subsidy	(175,937)	(78,002)
Adjustment related to the purchase of guaranteed loans	(732,768)	(363,881)
Other	(1,115)	2,733
Ending balance of the subsidy cost		
Allowance before reestimates	492,419	697,950
Add or subtract subsidy reestimates by component:		
Technical / default reestimate	2,051,080	535,453
Total of the above reestimate components	**2,051,080**	**535,453**
Ending balance of the loan guarantee liability	**$2,543,499**	**$1,233,403**

O. Administrative Expense:

(DOLLARS IN THOUSANDS)

FY 2003			
Direct Loan Programs	Total	Loan Guarantees Program	Total
(1) Business	$27,238	**Business**	$108,952
(2) Disaster	110,736		

P. Credit Program Receivables and Related Foreclosed Property (Summary of Notes 6B, 6C, 6H and 6I)

	FY 2003
Direct Loans Obligated Prior to FY 1992:	$92,163
Direct Loans Obligated After FY1991:	$2,693,012
Defaulted Guaranteed Loans from Pre-1992 Guarantees:	$214,924
Defaulted Guaranteed Loans from Post-1991 Guarantees:	$1,300,234
Credit Program Receivables and Related Foreclosed Property	$4,300,333

Q. Other Information:

Part J of this note, for pre-1992 business loans, relates to outstanding gross amounts guaranteed for FY 2003 of $742.5 million and for FY 2002 of $1.1 billion. Of this amount, the Agency's share for FY 2003 is $653.7 million and for FY 2002 is $939 million. For Pollution Control Equipment Contract Guarantee Fund (PCECGF), the outstanding guarantees for FY 2003 total $9.9 million and for FY 2002 total $12.2 million. This amount is both gross and Agency share. For post-1991 loans, the gross amount guaranteed for business loans for FY 2003 is $52.9 billion and for FY 2002 is $49 billion. The Agency's share is $42.7 billion for FY 2003 and $39.5 billion for FY 2002.

The SBA has outstanding loan commitments of $11.2 billion as of September 30, 2003, and $10.6 billion as of September 30, 2002. These figures are comprised entirely of post-1991 commitments.

The FY 2003 foreclosed property referred to in Parts B, C, H, and I is comprised of $19.9 million of real estate outstanding on 65 loans and $1.2 million of other property outstanding on 18 loans. The average number of days the outstanding foreclosed property was held by the SBA was 535 days. The number of items in process as of September 30, 2003 was 12.

R. Credit Program Subsidy:

SBA administers a number of loan guarantee and direct lending programs that provide financial assistance to small business not available in their financial markets. Under the loan guarantee programs, SBA guarantees loans to small businesses that are made by banks and other lending institutions. The loan guarantee programs include the 7(a) General Business Loan guarantee program, the Section 504 Certified Development Company loan guarantee program, the Small Business Investment Company Debentures and Participating Securities Programs, and the Microloan program. In the SBIC Participating Securities Program, SBA pays the interest to the holders of securities during the term of the security.

SBA's primary direct loan program is the Disaster program, which makes direct loans to disaster victims under 5 categories: (1) loans for homes and personal property, (2) physical disaster loans to businesses of any size, (3) pre-mitigation disaster loans to businesses, (4) economic injury loans to small businesses without credit available elsewhere, and (5) economic injury loans to eligible businesses affected by the call-up of an essential employee to active duty in the role of military reservist. A maximum interest rate of 4 percent is provided to applicants not having credit available elsewhere; the maximum is 8 percent for those with credit available elsewhere. Because SBA borrows at rates comparable to US Treasury Rates, there is a substantial interest rate subsidy in this program.

The Federal Credit Reform Act of 1990 (FCRA) requires that all agencies budget for the cost of credit programs by measuring the net present value of cash flows to and from the government. Loans originated during the same fiscal year are assigned to a "cohort" which is funded by appropriations for that year. Extensive amounts of transactional loan data and accounting data are used to model the forecasted cash flows for SBA programs, culminating in the development of a subsidy rate. OMB Circular A-11, provides direction on the preparation of credit program cost estimates, also known as subsidy rates.

The credit subsidy rate represents the present value cost to the government, expressed as a percentage of dollars of loan approvals, of each loan or loan guarantee program. The process to develop subsidy rate calculations is lengthy and complex, requiring unique data collection techniques and analysis efforts for each program. SBA develops its subsidy rates by creating models that incorporate data on loan maturity, borrowers' interest rates, fees, grace periods, interest subsidies, delinquencies, default or purchase rates, recoveries, prepayments and borrower characteristics.

The initial subsidy rates for loan cohorts are updated annually through subsidy re-estimates. Re-estimates that increase the subsidy rate involve the SBA's receipt of additional funds from Treasury, and re-estimates that decrease subsidy rates involve the transfer by SBA of subsidy funds back to the Treasury. For scheduling purposes, SBA may conduct these re-estimates using information as of March 31, which is then annualized.

Beginning in FY 1999 and continuing through FY 2003, SBA sold in bulk a large number of loans in seven sales. We have included information in Note (6) S of these statements regarding SBA's calculation of the gains and losses on these sales.

The subsidy rates for the 7(a) and the 504 programs have not changed significantly from the prior years due to the asset sale program. Disaster subsidy rates, however, have changed (increased) significantly, based on a revised evaluation of the asset sale program using a new disaster subsidy model built in FY 2003. The increased Disaster subsidy rates reflects both the revised cost of the disaster loans sold and other factors associated with the disaster program. SBA is therefore restating prior year results of asset sales for the disaster program. These amounts are included in FY 2003 re-estimates, and will be funded with permanent and indefinite authority granted under FCRA to the financing accounts (for post credit reform loans) and the liquidating accounts (for pre-credit reform loans).

Each subsidy rate represents the cost, as a percentage of the amount of guaranteed loans obligated in the cohort. Negative percentages indicate that the government currently expects a positive cash flow for that cohort.

Guarantee Programs

The 7(a) General Business Loan Guarantee Program

The following table shows the latest re-estimate of subsidy rates for the 7(a) program for all cohorts originated under the requirements of the FCRA. The total subsidy cost, presented on the left, is the sum of the components for the interest subsidy costs, default costs (net of recoveries), fees and other collections, and other costs.

Cohort Year	Original Subsidy Rate	FY 2003 Re-Estimate of Subsidy Rate and Components			
	Total	Total	Interest	Default	Fee/Other
1992	4.85	1.92	0	3.39	-1.47
1993	5.47	1.06	0	2.75	-1.69
1994	2.15	1.14	0	2.97	-1.83
1995	2.74	2.17	0	3.93	-1.76
1996	2.74	0.74	0	3.83	-3.09
1997	1.93	0.37	0	3.55	-3.18
1998	2.14	0.65	0	3.82	-3.17
1999	1.39	0.72	0	3.94	-3.22
2000	1.16	0.54	0	3.78	-3.24
2001	1.16	0.47	0	3.78	-3.31
2002	1.07	0.31	0	4.20	-3.89
2003	1.04	1.39	0	3.38	-1.99

Cohort Year	Original Subsidy Rate	FY 2002 Reestimate of Subsidy Rate and Components			
	Total	Total	Interest	Default	Fee/Other
1992	4.85	1.62	0	3.15	-1.53
1993	5.47	0.82	0	2.54	-1.71
1994	2.15	0.81	0	2.69	-1.88
1995	2.74	1.81	0	3.62	-1.81
1996	2.74	0.40	0	3.55	-3.15
1997	1.93	0.22	0	3.38	-3.16
1998	2.14	0.41	0	3.69	-3.28
1999	1.39	0.46	0	3.71	-3.25
2000	1.16	0.28	0	3.75	-3.47
2001	1.16	1.22	0	4.68	-3.46
2002	1.07	0.04	0	4.06	-4.02

7(a) loan performance is affected by economic conditions, legislation, credit origination and servicing policies, and various subsidy estimation methodologies and assumptions. During 2002 and 2003, default costs were higher than previously estimated. SBA management has attributed this outcome to the effect of the economy, particularly GDP and Unemployment. Fees decreased slightly from last year because of the increase in defaults.

504 Loans - The Certified Development Program

"The following table shows the latest re-estimate of subsidy rates for the 504 program for all cohorts originated under the requirements of the FCRA. The total subsidy cost is the sum of the components for the interest subsidy costs, default costs (net of recoveries), fees and other collections, and other costs. Each subsidy rate represents the cost, in the percentage of the guaranteed loans amount obligated in the cohort."

Cohort Year	Original Subsidy Rate	FY 2003 Re-Estimate of Subsidy Rate and Components			
	Total	Total	Interest	Default	Fee/Other
1992	0.49	3.68	0.00	3.53	0.15
1993	0.54	2.31	0.00	2.38	-0.07
1994	0.51	2.95	0.00	2.72	0.23
1995	0.57	2.85	0.00	3.48	-0.63
1996	0	2.16	0.00	3.50	-1.34
1997	0	-2.65	0.00	4.32	-6.97
1998	0	-3.34	0.00	3.66	-7.00
1999	0	-1.00	0.00	5.69	-6.70
2000	0	-0.93	0.00	4.97	-5.90
2001	0	-0.10	0.00	4.94	-5.04
2002	0	-0.02	0.00	4.00	-4.01
2003	0	0.45	0.00	4.19	-3.75

Cohort Year	Original Subsidy Rate	FY 2002 Re-Estimate of Subsidy Rate and Components			
	Total	Total	Interest	Default	Fee/Other
1992	0.49	3.65	0.00	3.53	0.12
1993	0.54	2.27	0.00	2.35	-0.08
1994	0.51	3.11	0.00	2.90	0.22
1995	0.57	2.98	0.00	3.66	-0.68
1996	0.00	2.36	0.00	3.78	-1.42
1997	0.00	-2.49	0.00	4.45	-6.94
1998	0.00	-2.07	0.00	4.59	-6.67
1999	0.00	-0.77	0.00	5.48	-6.26
2000	0.00	0.43	0.00	5.20	-4.78
2001	0.00	0.49	0.00	5.14	-4.65
2002	0.00	0.53	0.00	4.96	-4.43

The performance of the 504 guarantee program is affected by economic conditions, legislation, credit origination and servicing policies, and various subsidy estimation methodologies and assumptions. For most of the cohorts, the current re-estimated subsidy rates were lower than the previous year's reestimates because more cash from fees was available to offset a lower level of expected defaults.

Small Business Investment Companies – The Debentures Program

The following table shows the latest re-estimate of subsidy rates for the SBIC Debentures program for all cohorts originated under the requirements of the Federal Credit Reform Act. The total subsidy cost is the sum of the components for the interest subsidy costs, default costs (net of recoveries), fees and other collections, and other costs. SBA has prepared these estimates for loan guarantees in the current year's budget for the current and past years' cohorts. Each subsidy rate represents the cost, as the percentage of the guaranteed loans amount obligated in the cohort.

Cohort Year	**Original Subsidy Rate**	**FY 2003 Re-Estimate of Subsidy Rate and Components**			
	Total	**Total**	**Interest**	**Default**	**Fee/Other**
1992	14.29	10.18	0	11.09	-0.91
1993	15.40	4.55	0	5.46	-0.91
1994	16.25	5.33	0	6.75	-1.42
1995	14.65	4.85	0	6.38	-1.54
1996	15.46	15.16	0	16.69	-1.54
1997	3.19	5.14	0	13.19	-8.05
1998	1.94	12.39	0	20.90	-8.51
1999	1.38	1.36	0	10.85	-9.49
2000	0.00	-3.90	0	6.77	-10.67
2001	0.00	-3.85	0	6.60	-10.44
2002	0.00	-3.48	0	7.22	-10.70
2003	0.00	1.84	0	12.58	-10.73

Cohort Year	Original Subsidy Rate	FY 2002 Re-Estimate of Subsidy Rate and Compnents			
	Total	Total	Interest	Default	Fee/Other
1992	14.29	16.01	0	16.92	-0.91
1993	15.4	9.62	0	10.54	-0.91
1994	16.25	0.37	0	1.79	-1.42
1995	14.65	-0.34	0	1.19	-1.54
1996	15.46	1.35	0	2.89	-1.54
1997	3.19	-4.23	0	4.72	-8.95
1998	1.94	-0.24	0	9.89	-10.12
1999	1.38	2.63	0	12.72	-10.1
2000	0	-2.1	0	8.76	-10.86
2001	0	-2.02	0	8.87	-10.89
2002	0	-2.09	0	9.15	-11.24

The performance of the SBIC debenture guarantee program is affected by economic conditions, legislation, credit origination and, various subsidy rate estimation methodologies and assumptions.

In 2001, legislation was enacted allowing the fee on this program to adjust every year in order to reach a rate of zero. Once established, these fees remain the same for the life of each cohort. During FY 2003, the subsidy rose because default costs rose as larger than estimated defaults occurred in one group of cohorts.

As described further below, the venture capital industry, which the SBIC program serves, has experienced a substantial economic downturn over the past several years. This downturn has likewise affected the SBIC program. For the purpose of forecasting expected defaults and other cash flows in the relatively near future (FY04-FY06), SBA determined that a review of the Agency's actual SBIC portfolio would be more accurate that relying purely on a long tern historical experience as has traditionally been done. Therefore the re-estimates above include SBA's estimate of likely defaults based on a portfolio review for FY04-FY06. Long term average defaults were used for all post-FY06 cash flows.

Small Business Investment Companies – The Participating Securities Program

The following table shows the latest re-estimate of subsidy rates for the SBIC Participating Securities program for all cohorts originated under the requirements of the FCRA. The total subsidy cost is the sum of the components for the interest subsidy costs, default costs (net of recoveries), fees and other collections, and other costs. SBA has prepared these estimates for loan guarantees in the current year's budget for the current and past years' cohorts. Each subsidy rate represents the cost, as a percentage of the guaranteed loans amount obligated in the cohort.

Cohort Year	Original Subsidy Rate	FY 2003 Re-Estimate of Subsidy Rate and Components			
	Total	Total	Interest	Default	Fee/Other
1994	9.00	-14.02	0.00	3.81	-17.83
1995	8.90	3.25	0.00	10.65	-7.40
1996	9.00	5.26	0.00	14.16	-8.90
1997	3.29	21.69	0.00	25.81	-4.12
1998	2.20	25.05	1.27	27.58	-3.80
1999	2.19	49.32	1.16	41.00	7.16
2000	1.80	47.75	2.06	39.60	6.09
2001	1.31	29.57	0.00	26.22	3.35
2002	0.00	22.06	0.00	20.09	1.97
2003	0.00	25.98	0.00	24.05	1.93

Cohort Year	Original Subsidy Rate	FY 2002 Re-Estimate of Subsidy Rate and Components			
	Total	Total	Interest	Default	Fee/Other
1994	9	-15.19	0	1.47	-16.66
1995	8.9	-4.19	0	6.13	-10.31
1996	9	-6.68	0	6.88	-13.56
1997	3.29	5.11	0	12.64	-7.53
1998	2.2	3.85	0	9.88	-6.03
1999	2.19	10.6	0	8.96	-7.82
2000	1.8	4.15	0	8.48	-4.34
2001	1.31	-4.89	0	7.1	-11.99
2002	0	-4.24	0	7.01	-11.25

In 2001, legislation was enacted allowing the fee on the SBIC Participating Security program to adjust at the beginning of the cohort in order to reach an estimated rate of zero. Once established, these fees remain the same for the life of each cohort. During FY 2003, the subsidy rates increased because default costs were substantially larger than estimated defaults across all cohorts.

As described in the SBIC Debentures section above, the venture capital industry, which the SBIC program serves, has experienced a substantial economic downturn over the past several years. This downturn is particularly evident in the SBIC Participating Securities program. Therefore the re-estimates above include SBA's estimate of likely defaults based on a portfolio review for FY04-FY06. Long term average defaults were used for all post-FY06 cash flows.

The re-estimates also include a reduction in the SBA's assumption regarding likely recoveries on the defaulted guarantees. SBA had previously assumed approximately 60% of the defaulted amounts would be recovered. SBA has now reduced this estimate to 35% based on the program managers' professional judgment, given the type of assets being liquidated.

Given the inherent volatility of venture capital investments, although these are SBA's best estimates at this time of the probable levels of defaults and recoveries, many different events that cannot be accurately foreseen, including the performance of the economy and especially the stock market, may have a significant impact on the ultimate cost of the program.

In addition, several modifications to the data processing methodology resulted in many of the cohorts reflecting either an upward or downward adjustment.

Direct Loan Programs

The Disaster Loan Program

The following table shows the latest re-estimate of subsidy rates for the Disaster Loan program for all cohorts originated under the requirements of the Federal Credit Reform Act. The total subsidy cost is the sum of the components for the interest subsidy costs, default costs (net of recoveries), and other collections, and other costs. Each subsidy rate represents the cost, as a percentage of the amount of direct loans obligated in the cohort.

During FY 2003, SBA revised its modeling methodology for the Disaster Program. The new model was intended to provide a common basis for estimates, re-estimates and, as necessary, loan valuations for asset sales. This new model is the basis for the FY 2003 re-estimates. For comparison, the chart also shows re-estimates that would have been shown in the FY 2002 Financial Statements had this model been available for use at the time that the FY 2002 statements were produced. These restated rates are reflected in the restated FY2002 Financial Statements.

Cohort Year	Original Subsidy Rate	FY 2003 Reestimate of Subsidy Rate	FY 2002 Reestimate of Subsidy Rate
	Total	Total	Total
1992	33.93	36.59	37.1
1993	20.58	31.01	31.5
1994	22.99	26.54	26.95
1995	31.54	26.52	27.06
1996	28.08	27.38	27.91
1997	20.02	30.93	31.72
1998	23.46	25.60	26.43
1999	22.36	22.93	21.53
2000	22.2	20.69	18.49
2001	17.46	14.54	13.67
2002	14.67	13.88	
2003	13.98		

1. This cohort was not restated for the prior year.

The cost of this direct loan program is affected by the original terms of the loan such as interest rates, grace periods and average loan size. Deviations from the original terms caused by prepayments, defaults, delinquencies, charge-offs, and recoveries can have a significant effect of the cost. Generally, these can be caused by legislation, credit origination and servicing policies.

S. Loan Asset Sales:

Beginning in FY 1999, SBA has conducted seven loan asset sales. Disaster, 7(a), 504, and other loans were sold over the course of the program. Asset Sale #7 occurred in FY 2003 and asset sales # 5 and #6 sales occurred in FY 2002. At the time of the sales, SBA used its OMB-approved “hold models” to estimate the “value to government” of holding the loans. This estimate was used as a threshold for determining whether or not to sell the loans based on the bids received in the sales. For each of the seven sales that SBA conducted, the proceeds of the sales exceeded the “value to government” estimate that had been calculated prior to the sale, so with OMB’s approval, SBA sold the loans.

In January, 2003 SBA determined that its previous “value to government” estimation methodology was inconsistent with its subsidy model methodology. As a result, SBA temporarily suspended the asset sales program until the problem could be resolved. During FY 2003, SBA built a new Disaster loan subsidy model with the functionality to calculate both the subsidy budget cost of the loan program and the “value to government” (or book value) of individual loans. SBA used this new model to calculate new book value estimates for all Disaster loans sold in the asset sales program. The new model was also used to calculate reestimates for the Disaster program. Overall, SBA found that the old Disaster subsidy model had under estimated the cost of the program by 3.6 % on average. SBA also found that the previous “hold model” had consistently under valued the loans that were sold in the asset sales by about 30 percent. SBA’s new Disaster loan model indicates that SBA lost a total of $909 million on the Disaster loan sales.
Since SBA had also developed separate models to estimate the value to government of the 7(a) and 504 loans sold in

the asset sales, SBA was concerned that those estimates could be inconsistent with the results of the subsidy budget models for those programs. Consequently, SBA recalculated the value to government for the 7(a) and 504 loans using the recovery assumptions from the subsidy models in place at the time the loan sales were completed. SBA then used those updated value to government estimates as the book values of the loans for accounting purposes.

The final results of the loan sales by program and sale are shown in the following table. Positive values represent gains to the government while negative numbers represent losses.

Gain / Loss By Sale

(DOLLARS IN MILLIONS)

	Total	Sale 1 Aug-99	Sale 2 Aug-00	Sale 3 Dec-00	Sale 4 Aug-01	Sale 5 Jan-02	Sale 6 Aug 02	Sale 7 Dec-02	Sale 8
7a	$22	$28	$13	$3	$2	$(6)	$(10)	$(7)	$(1)
Disaster	(909)		(365)	(171)	(128)	(72)	(79)	(79)	(15)
504	50	39	1		3	2	1	5	(1)
Other	9	10	(1)						
Total	**$(828)**	**$77**	**$(352)**	**$(168)**	**$(123)**	**$(76)**	**$(88)**	**$(81)**	**$(17)**

Although the SBA did not complete Asset Sale #8, $16 million in expenses were incurred in preparation for the sale as shown in the table above. These expenses were applied as a reduction to the proceeds of Asset Sale #7.

SBA's original methodology for adjusting the book value of the loans sold in its accounting system was independent of the value to government estimates calculated by the new hold models. After review, this methodology is now deemed to be erroneous. The SBA has corrected the book values in its accounting system to be consistent with the "hold" values calculated by the new model. The final gain (loss) on the sales by program is shown in the table below.

(DOLLARS IN MILLIONS)

Program	Number of Loans Sold	UPB	New Book Value	Net Proceeds	New Gain / Loss	Old Gain / Loss	Gain / Loss Change
7(a)	4,400	506	156	178	22	-141	163
Disaster	158,680	4,912	3,957	3,048	-909	-1,549	640
504	954	201	42	91	50	-76	126
Other	1,899	96	54	63	9	-9	19
Total	**165,933**	**5,715**	**4,208**	**3,380**	**-828**	**-1,775**	**947**

The net proceeds amount shown in the table includes expenses from Sales 1-8. In addition, SBA had reserved a total of $82 million (across all sales) for representation and warranty purposes which SBA has now determined will not be necessary for investor claims. Therefore, the $82 million has been deducted from the asset sale expenses and the net proceeds amount has been increased to include it.

As shown in the chart, using the new methodologies, SBA now calculates a total loss on sales of $828 million, which is $947 million less than the previously recorded loss of $1,775 million. Although this footnote contains the disclosure of the changes in the book value and related gain and loss, these changes have no impact on the principal financial statements because the adjusting entries effectively offset each other. The decrease in book value resulted in a debit to the allowance for subsidy (or the payable to Treasury for loans sold from the Liquidating Accounts) and a credit to loan principal. The decrease in the loss on sale resulted in a debit to principal and a credit to the allowance for subsidy (or payable to Treasury). The net result is no change to principal or allowance for subsidy.

NOTE 7. General Property and Equipment

(DOLLARS IN THOUSANDS)

FY 2003

Major Classes	Cost	Amortization	Net Book Value
Internal Use Software in Development	$4,870		$4,870
Internal Use Software	9,191	(5,539)	3,652
	$14,061	$(5,539)	$8,522

(Dollars in Thousands)

FY 2002

Major Classes	Cost		Net Book Value
Internal Use Software in Development	$1,786		$1,786
Internal Use Software	7,563	(2,521)	5,042
	$9,349	**$(2,521)**	**$6,828**

NOTE 8. Advances and Other Assets

(DOLLARS IN THOUSANDS)

	FY 2003		FY 2002 - Restated	
	Intragovernmental	Public	Intragovernmental	Public
Asset Sale Costs				$23,287
Advances from Program Funds	$49,476		$60,152	
Sub-Total before Eliminations	**$49,476**		**$60,152**	**$23,287**
Eliminations	(49,476)		(60,152)	
Balance Sheet Total				**$23,287**

For FY 2003 reporting, the SBA has reclassified accounts no longer considered as advances. These are Advances to Federal Financing Bank - Section 503 Debentures, Advances to Holders of Delinquent Payments - Section 504 Debentures, Advances to Private Investors - SBIC Debentures, Advances to Receivers - SBIC Debentures and Loans and Advances Outstanding - SBIC Participating Securities. Also, for FY 2003 reporting, the SBA now includes the account Other Assets - Asset Sale Specific Costs as an advance.

NOTE 9. Liabilities Not Covered by Budgetary Resources

(DOLLARS IN THOUSANDS)

	FY 2003	FY 2002 - Restated
Intragovernmental		
Other		
Salaries and Expenses	$5,708	$5,470
Total Intragovernmental	**$5,708**	**$5,470**

The Salaries and Expenses amount is the FECA liability.

Other Liabilities- Public Not Covered by Budgetary Resources

	FY 2003	FY 2002 - Restated
FECA Actuarial Liability (Note 11)	$31,822	$31,487
Other		
Business Loan and Investment Fund	$1,682	$395
Disaster Loan Fund	26	226
Salaries and Expenses	21,894	21,244
Total	**$23,602**	**$21,865**
Total Other Liabilities - Public Not Covered by Budgetary Resources	**$55,424**	**$53,352**

Other for Business Loan and Investment Fund and Disaster Loan Fund is Prior Liens Outstanding on Acquired Collateral. The Salaries and Expenses amount is annual leave for all SBA employees.

NOTE 10. Debt

(DOLLARS IN THOUSANDS)

FY 2003

	Beginning Balance	New Borrowings	Repayments	Change in Interest Payable	Ending Balance
Intragovernmental Debt:					
Borrowing from the Treasury	$11,035,897	$1,158,196	($5,567,308)	($36)	$6,626,749
Borrowing from Federa Financing Bank	105,487		(25,106)	(751)	79,630
Total Intragovern-mental Debt	**$11,141,384**	**$1,158,196**	**($5,592,414)**	**($787)**	**$6,706,379**

FY 2002 - Restated

	Beginning Balance	New Borrowings	Repayments	Change in Interest Payable	Ending Balance
Intragovernmental Debt:					
Borrowing from the Treasury	$10,719,331	$2,451,887	($1,502,479)	($632,842)	$11,035,897
Borrowing from Fed-eral Financing Bank	131,964		(29,545)	3,068	105,487
Total Intragovern-mental Debt	**$10,851,295**	**$2,451,887**	**($629,774)**	**($629,774)**	**$11,141,384**

NOTE 11. FECA Actuarial Liability

The future workers' compensation estimates are generated from an application of actuarial procedures developed to estimate the liability for FECA benefits. The FECA actuarial liability includes the present value of the expected liability for employee death, disability, medical, and miscellaneous costs for approved compensation cases. It is estimated using the paid-losses extrapolation method calculated over the next 23 years. This method uses historical benefit payment patterns related to a specific incurred period to predict the entire payments related to that period. This is a non-current liability "non-intragovernmental" not covered by budgetary resources. The FY 2003 liability is $31.8 million and the FY 2002 liability is $31.5 million.

NOTE 12. Other Liabilities

(DOLLARS IN THOUSANDS)

FY 2003

	Non-Current Liabilities	Current Liabilities	Total Liabilities
1. Intragovernmental			
Payable to Special Receipt Fund	$	$208,832	$208,832
Modification Adjustment Transfer		214,752	214,752
Employment Taxes Payable		196	196
Unfunded FECA Liability		5,707	5,707
Due Federal Financing Bank	1,855		1,855
Net Assets of Liquidating Funds Due to Treasury	407,109		407,109
Advances from Other Agencies		1,945	1,945
Advances from Program Fund		49,476	49,476
Sub-Total before Eliminations	**$408,964**	**$480,908**	**$889,872**
Eliminations		(49,476)	(49,476)
Total Intragovernmental Liabilities - Other	**$408,964**	**$431,432**	**$840,396**
2. Liabilities - Public			
Accrued Funded Payroll Benefits	$	$8,909	$8,909
Accrued Grants		39,700	39,700
Accrued Unfunded Annual Leave		21,894	21,894
Employment Taxes Payable		2,244	2,244
Advances From Others		502	502
Cash Adjustments		18,178	18,178
Suspense Accounts		(4,998)	(4,998)
Prior liens on Real Estate	1,708		1,708
Deferred Credits - Interest Income	32,197		32,197
Contingent Liabilities	19,154	800	19,954
Total Public Liabilities - Other	**$53,059**	**$87,229**	**$140,288**

FY 2002 - Restated

	Non-Current Liabilities	Current Liabilities	Total Liabilities
1. Intragovernmental			
Payable to Special Receipt Fund	$	$295,416	$295,416
Modification Adjustment Transfer		151,577	151,577
Employment Taxes Payable		854	854
Unfunded FECA Liability		5,469	5,469
Due Federal Financing Bank	2,416		2,416
Net Assets of Liquidating Funds Due to Treasury	762,403		762,403
Advances from Other Agencies		1,378	1,378
Advances from Program Fund		60,152	60,152
Sub-Total before Eliminations	**$764,819**	**$514,846**	**$1,279,665**
Eliminations		(60,152)	(60,152)
Total Intragovernmental Liabilities - Other	**$764,819**	**$454,694**	**$1,219,513**

2. Liabilities - Public			
Accrued Funded Payroll Benefits	$	$6,207	$6,207
Accrued Unfunded Annual Leave		21,244	21,244
Employment Taxes Payable			
Advances From Others		594	594
Cash Adjustments		18,178	18,178
Suspense Accounts		7,553	7,553
Prior liens on Real Estate	620		620
Deferred Credits - Interest Income	48,010		48,010
Grant Accrual	39,700		39,700
Contingent Liabilities	14,527	800	15,327
Total Public Liabilities - Other	**$102,857**	**$54,576**	**$157,433**

SBA recorded a contingent liability of $800,000 for claims that were reasonably possible to be realized. The SBA has estimated that its ultimate losses for contingent liabilities for other claims related to various administrative proceedings, legal actions, environmental suits, and claims brought against it may range from zero to $35 million.

The SBA has recorded a non-current contingent liability for future claims in its Surety Bond Program in the amount of $19,154 million for FY 2003 and $14,527 million for FY 2002. This liability is an estimate of the future requirement for claims should the program cease operations.

NOTE 13. Statement of Net Cost

Federal cost accounting standards require the SBA to report operating costs by program activity. Full costs include all direct and indirect costs consumed by a program. Full costs are reduced by exchange (earned) revenues to arrive at net operating cost.

1. Operating Cost

The full and net operating costs of the SBA's major programs are presented in the Consolidated Statement of Net Cost. Full program costs are comprised of all direct costs consumed by the program and those indirect costs which can be reasonably assigned or allocated to the program, including employee pension and other retirement benefit costs paid by the OPM and imputed by the SBA.

2. Earned Revenue

Earned revenues arise from exchange transactions which occur through the provision of goods and services for a price, and are deducted from the full cost of the SBA's major programs to arrive at net program cost. Earned revenues are recognized by the SBA when reimbursements are payable from other Federal agencies and from the public, as a result of costs incurred or services performed on their behalf. A major source of earned revenue includes interest earned on the SBA's outstanding Business and Disaster loan portfolios.

3. Costs Not Assigned

Costs Not Assigned are costs the Agency has determined are not properly allocable to programs such as the Office of Inspector General, Congressional Initiatives, and some grants for FY 2002.

4. Earned Revenue Not Attributed to Programs

Earned Revenue Not Attributed to Programs are revenues the Agency has determined are not properly allocable to programs such as the Office of Inspector General.

(DOLLARS IN THOUSANDS)

	2003	Eliminations	Consolidated	2002 Restated
Champion Small Business Interests				
Intragovernmental				
Gross Costs	$2,951		$2,951	$3,453
Less: Earned Revenue				
Net Costs	**$2,951**		**$2,951**	**$3,453**
Public				
Gross Costs	$10,984		$10,984	$14,732
Less: Earned Revenue				
Net Costs	**$10,984**		**$10,984**	**$14,732**
Net Cost of Champion Small Business Interests	**$13,935**		**$13,935**	**$18,185**
Empowering Entrepreneurs				
Intragovernmental				
Gross Costs	$214,677	($136,190)	$78,487	($8,004)
Less: Earned Revenue	53,335		53,335	32,148
Net Costs	**$161,342**	**($136,190)**	**$25,152**	**($40,152)**
Public				
Gross Costs	$3,153,943		$3,153,943	$1,113,346
Less: Earned Revenue	499,401		499,401	188,576
Net Costs	**$2,654,542**		**$2,654,542**	**$924,770**
Net Cost of Empowering Entrepreneurs	**$2,815,884**	**($136,190)**	**$2,679,694**	**$884,618**
Disaster Programs				
Intragovernmental				
Gross Costs	$645,207	($110,736)	$534,471	$684,008
Less: Earned Revenue	281,724		281,724	435,879
Net Costs	**$363,483**	**($110,736)**	**$252,747**	**$248,129**
Public				
Gross Costs	$396,915		$396,915	$654,635
Less: Earned Revenue	224,490		224,490	258,259
Net Costs	**$172,425**		**$172,425**	**$396,376**
Net Cost of Disaster Programs	**$535,908**	**($110,736)**	**$425,172**	**$644,505**
Cost not assigned to programs	$54,508		$54,508	$41,046
Less: Earned revenue not attributed to programs	248,554	(246,926)	1,628	(285)
Net Cost not assigned to Programs	**($194,046)**	**$246,926**	**$52,880**	**$41,331**

FY 2003			
	Gross Cost Net Cost	Earned Revenue	Net Cost
Functional Classification			
Commerce and Housing Credit	$3,246,365	$552,736	$2,693,629
Community and Regional Development	985,894	507,842	478,052
Total	**$4,232,259**	**$1,060,578**	**$3,171,681**

FY 2002 - Restated			
	Gross Cost Net Cost	Earned Revenue	Net Cost
Functional Classification			
Commerce and Housing Credit	$1,123,527	$243,249	$880,278
Community and Regional Development	1,379,689	671,328	708,361
Total	**$2,503,216**	**$914,577**	**$1,588,639**

Intragovernmental Revenue

FY 2003		
Functional Classification		
Commerce and Housing Credit	$	$53,335
Community and Regional Development		283,994
Total	**$**	**$337,329**
Champion Small Business Interests		
Intragovernmental Gross Costs		
Office of Advocacy	$17,02	$15,39
Ombudsman	220	588
Office of Veterans' Affairs	316	438
Women's Business Council	233	125
International Trade Promotion	398	575
Egypt Reimbursed Expense		188
USAID - Nigeria	55	
International Visitors Program	27	
Gross Costs	**$2,951**	**$3,453**
Less: Earned Revenue		
Net Costs	**$2,951**	**$3,453**
Public Gross Costs		
Office of Advocacy	$6,335	$6,565
Ombudsman	817	2,509
Office of Veterans' Affairs	1,175	1,868
Women's Business Council	869	534
International Trade Promotion	1,482	2,455
Egypt Reimbursed Expense		801
USAID - Nigeria	204	
International Visitors Program	102	
Gross Costs	**$10,984**	**$14,732**
Less: Earned Revenue		
Net Costs	**$10,984**	**$14,732**
Total Net Cost	**$13,935**	**$18,185**

Empowering Entrepreneurs

	2003	2002 - Restated
Business Loan Programs		
Intragovernmental		
Gross Costs	$172,015	$85,950
Less: Earned Revenue	51,577	31,385
Net Costs	**$120,438**	**$54,565**
Public		
Gross Costs	$691,607	$337,721
Less: Earned Revenue	163,280	97,784
Net Costs	**$528,327**	**$239,937**
Total Net Cost	**$648,765**	**$294,502**

Development Company Programs		
Intragovernmental		
Gross Costs	$(36,053)	$5,549
Less: Earned Revenue	(716)	314
Net Costs	**$(35,337)**	**$52,35**
Public		
Gross Costs	$33,168	$40,427
Less: Earned Revenue	11,415	34,354
Net Costs	**$21,753**	**$6,073**
Total Net Cost	**$(13,584)**	**$11,308**
Small Business Investment Company (SBIC) Programs		
Intragovernmental		
Gross Costs	$25,924	$(31,629)
Less: Earned Revenue	2,474	449
Net Costs	$23,450	$(32,078)
Public		
Gross Costs	$2,195,366	$396,036
Less: Earned Revenue	319,008	52,084
Net Costs	**$1,876,358**	**$343,952**
Total Net Cost	**$1,899,808**	**$311,874**
Secondary Market Guaranty		
Intragovernmental		
Gross Costs		
Less: Earned Revenue		
Net Costs		
Public		
Gross Costs	$24,683	$123,452
Less: Earned Revenue		
Net Costs	**$24,683**	**$123,452**
Total Net Cost	**$24,683**	**$123,452**
Surety Bond Guarantees Programs		
Intragovernmental		
Gross Costs	$2,621	$888
Less: Earned Revenue		
Net Costs	**$2,621**	**$888**

Public		
Gross Costs	$22,332	$10,431
Less: Earned Revenue	5,698	4,354
Net Costs	**$16,634**	**$6,077**
Total Net Cost	**$19,255**	**$6,965**
Business Development Programs		
Intragovernmental		
Gross Costs	$9,853	$12,359
Less: Earned Revenue		
Net Costs	**$9,853**	**$12,359**
Public		
Gross Costs	$36,683	$52,734
Less: Earned Revenue		
Net Costs	**$36,683**	**$52,734**
Total Net Cost	**$46,536**	**$65,093**
Government Contracting Programs		
Intragovernmental		
Gross Costs	$5,640	$5,104
Less: Earned Revenue		
Net Costs	**$5,640**	**$5,104**
Public		
Gross Costs	$20,998	$21,777
Less: Earned Revenue		
Net Costs	**$20,998**	**$21,777**
Total Net Cost	**$26,638**	**$26,881**
Entrepreneurial Development Programs		
Intragovernmental		
Gross Costs	$34,677	$30,647
Less: Earned Revenue		
Net Costs	**$34,677**	**$30,647**
Public		
Gross Costs	$129,106	$130,768
Less: Earned Revenue		
Net Costs	**$129,106**	**$130,768**
Total Net Cost	$163,783	$161,415

Empowering Entrepreneurs

Intragovernmental		
Gross Costs	$214,677	$108,868
Less: Earned Revenue	53,335	32,148
Net Costs	**$161,342**	**$76,720**
Public		
Gross Costs	$3,153,943	$1,113,346
Less: Earned Revenue	499401	188,576
Net Costs	$2,654,542	$924,770
Total Net Cost	$2,815,884	$1,001,490

NOTE 14. Disclosures Related to the Statement of Changes in Net Position

The SBA's net position, as of September 30, 2003, consisted of the following:

1. Unexpended Appropriations

Unexpended appropriations represent (1) unobligated amounts and (2) amounts for which orders for goods, services or benefits, have been placed, but not yet filled. Multi-year appropriations remain available to the SBA for obligation in future periods. Unobligated balances associated with appropriations that expire at the end of the fiscal year remain available for obligation adjustments, but not new obligations, until that account is closed, five years after the appropriations expire.

The SBA's unexpended appropriations beginning balance was restated on the FY 2002 statement by ($6.843) million to cover period adjustments. These prior period adjustments were made to reflect the accrual for grants and Administrative Accounting corrections for Oracle Agency Location Code assignments on advances and earned reimbursements.

2. Cumulative Results of Operations

Cumulative results of operations is the accumulated difference between expenses and financing sources since the inception of the SBA.

The SBA restated the Cumulative Results of Operations beginning balance by ($825.455) million to cover prior period adjustments. These prior period adjustments were made to reflect the changes in accounting for disaster re-estimates and Administrative Accounting corrections for Oracle Agency Location Code assignments on advances and earned reimbursements.

NOTE 15. Disclosures Related to the Statement of Budgetary Resources

The Budget of the United States, the President's Budget, with actual numbers for the Fiscal Year 2003 has not yet been published. It is expected to be published February, 2004 and will be available via the internet at www.firstgov.gov or via written or telephone request to Office of Citizen Services and Communications, U.S. General Services Administration, 1800 F Street, NW Washington, DC 20405, 1-800-333-4636.

For the Fiscal Year 2003, the material difference between the amounts reported on the Statement of Budgetary Resources (SBR) and the SF-133 are as follows:

Report Line	Line Name	SBR	Budget Execution	Difference	Explanation
2A	Unobligated Balance Brought Forward	6,761,781	6,740,317	21,464	Budgetary account change in recording Disallowed Purchased Interest Liability
3A	Spending Authority from Offsetting Collections Earned	3,450,849	3,403,442	47,407	25M - General ledger account correction - Federal Financing Bank Transactions
					55M - Asset Sales - Change in budgetary accounting entry for various trancodes
					20M - Accounting change for Suspense Allocation recordation
					negative 48M - Accounting change for recording Other Federal Receivables
					negative 5M - program fund advances to Administrative fund
4	Recoveries of Prior Year Obligations	211,529	148,328	63,201	Asset Sales adjustments

8	Obligations Incurred	5,320,815	5,221,033	99,782	20M - Accounting change for Suspense Allocation recordation 25M - General ledger account correction - Federal Financing Bank Transactions 55M - Asset Sales adjustments
10	Unobligated Balances	660,519	638,253	22,266	Additional FAIC interest due treasury due to change in Asset Sales treatment
12	Unobligated Balance Beginning of Period	730,959	752,423	(21,464)	Budgetary account change in recording Disallowed Purchased Interest Liability
14C	Undelivered Orders	643,939	683,775	(39,836)	Grant accrual

For the Fiscal Year 2002, several line items on the SBR were different from comparable line items on the Budget of the United States Government (BUSG). The SBA had not accumulated all of the information it needed prior to the submission deadline of BUSG data. Missing from the SBA's BUSG submission was an erroneous entry in FACTS II during the revision period to correct the reporting of Asset Sales activity ($34 million-Disaster program), an audit adjustment for Asset Sales corrections ($17 million-Disaster program and $50 million BLIF) and $287 million adjustment to the Liquidating Fund for a change in the estimation of the Guaranty Liability. Additional differences were the result of gathering data from different sources. The SBR was prepared using data from the Agency's general ledger, while some of the BUSG data was obtained from internal costs reports. Lastly, the SBA's SBR splits its unobligated balances between "Available" and "Not Yet Available" and the BUSG does not.

SBA had no borrowing or contract authority at the end of FY 2003 or 2002. Repayments of borrowings are made annually from collections received through the SBA's credit reform portfolio. Borrowing repayments are calculated using the guidance provided by OMB. The SBA has access to permanent indefinite appropriations for liquidating fund obligations and upward subsidy reestimates.

During FY 2003 the SBA incurred $5.321 billion of direct obligations of which $1.442 billion was apportioned by fiscal quarters (type A apportionment) and the $3.879 billion was apportioned by fiscal year for (type B apportionment).

NOTE 16. Disclosures Related to the Statement of Financing

Imputed Financing includes an imputed cost of $7.41 million for pension benefits, $11.615 million for health benefits and $38 thousand for life insurance.

The Balance Sheet reflects the account balances for liabilities not covered by budgetary resources as described in Note 9. The Statement of Financing reflects changes from period-to-period in those unfunded liabilities in the section titled "Components of the net cost of operations that will not require or generate resources in the current period".

NOTE 17. Disclosure Related to Restatement of FY 2002 Financial Statements

Issue 1: Subsidy Reestimate

The SBA used a New Disaster subsidy model for the FY 2003 reestimate of the cost of its Disaster loans made since FY 1992. The new Disaster subsidy model develops cashflow projections using the status and remaining term of each Disaster loan, as opposed to the average composite loans used in the old Disaster model. As a result, the new model provides an improved forecast of Disaster loan defaults and recoveries and a much improved estimate of loan subsidy cost for Disaster loans outstanding and the impact of the SBA's loan asset sales which corrects errors in reestimated amounts caused by the previous model. Using this new model the SBA's estimate of Disaster program costs substantially increased, and the SBA is restating its FY 2002 financial statements to include these increased costs as a correction to the statements.

Issue 2: Master Reserve Fund

The SBA used a new model in FY 2003 to compute the status for its 7(a) Master Reserve Fund (MRF) balance (see footnote 4). The new model uses the MRF balance and the status of individual loans in the MRF along with the SBA's experience on 7(a) loan cashflow to project the adequacy of the MRF. Previously, the SBA's estimate was based on a projection of the results of the MRF balance for closed pools of 7(a) loans. The new model provides a much improved estimate of the adequacy of the MRF to meet its future obligations. Using the new MRF model, upward reestimates for both FY 2002 and FY 2003 were calculated and recorded. The SBA has restated its FY 2002 financial statements to eliminate the previous error and record the proper reestimate.

Issue 3: Revision of Pre-1992 Guarantee Loan Liability

During the FY 2002 audit a determination was made that the SBA lacked a calculation methodology for reasonably calculating a guarantee liability for pre-Credit Reform guarantees. The SBA revamped this methodology in FY 2003 by applying subsidy recovery rates in its calculations and by better defining and documenting the estimation process. The improved methodology was used to adjust the incorrect FY 2002 amounts which are part of the restated financial statements.

Issue 4: Administrative Accounting Changes

The SBA corrected some budgetary balances and also corrected Agency Location Codes on advances and earned reimbursements. The corrections of these errors are reflected in the restated FY 2002 statements.

Issue 5: Change in Presentation - Advances

The SBA advances interest due to holders of SBIC debentures and participating securities. As a result of FY 2002 audit findings, the SBA has changed the presentation of these SBIC advances to more accurately reflect the nature of the underlying activity according to our current understanding by including them with credit program receivables. As of this change, the SBA also adjusted its allowance for subsidy to show reasonable valuation of the credit program receivables. The restated Balance Sheet reflects the results of this change.

Issue 6: Change in Presentation - Other Asset - Sale Costs

The SBA determined that the nature of this asset was more closely related to credit program receivables than to advances and has changed the Balance Sheet presentation for FY 2002.

Issue 7: Change in Proforma for Recordation of Upward Adjustments of Prior-Year Undelivered Orders

The SBA corrected an account number error in an automated proforma accounting entry. The FY 2002 statements have been adjusted to reflect the correction.

Issue 8: Change in Proforma for Recordation of Guarantee Purchases

The SBA determined that an entry required adjustment to reflect current business practices. The proforma entry incorrectly contained a revenue account when it should have used an expense account. The correction resulted in offsetting changes to both revenue and expenses on the Statement of Net Cost for FY 2002.

Issue 9: Change in Grant Accruals

For FY 2003 reporting, the SBA developed a process to estimate the amount of unrecorded payments outstanding grants for the Small Business Development Company program as well as other grant activity. In addition, the SBA utilized the methodolgy to correct the accruals for restatement on its FY 2002 financial statements.

Issue 10: Change in Proforma for Federal Financing Bank Transactions

The SBA corrected a general ledger account number error in a proforma entry to record an accounting event related to the Federal Financing Bank. The result is an offsetting change to collections and disbursements for the FY 2002 Statement of Budgetary Resources and the Statement of Financing.

Issue 11: Change in Aging of Receivables

During FY 2003, the SBA improved the subsidiary system used to determine delinquent interest on its loans for financial reporting purposes. This improvement allowed correction to the amount of delinquent interest for FY 2002 reporting. The SBA is restating its FY 2002 financial report to include this correction.

Issue 12: Change in Disallowed Purchased Interest

This change is closely allied to the change in issue 8. Analysis revealed that the SBA was overstating a liability related to disallowed purchased interest; accordingly the liability was adjusted for reporting purposes on the Balance Sheet from FY 2002. The resulting budgetary account changes are reflected on the Statement of Budgetary Resources for FY 2002.

Issue 13: Correction to Allowance for Subsidy

During FY 2003 the SBA developed an estimate for recoveries on defaulted principal receivable in its SBIC program. The estimate enabled the establishment of an Allowance for Subsidy related to the defaulted principal. This same methodolgy was used to correct the omission of an allowance for FY 2002. This correction is in the restated Balance Sheet for FY 2002.

Below is a summary of the items by principal statement that were restated for FY 2002. The issue number corresponds to the issue number directly above.

Balance Sheet

(DOLLARS IN THOUSANDS)

	Issue	As Reported	Adjustment	Restated
Advances - Intragovernmental	5	4,428	(4,428)	0
Credit Program Receivables	1		(971,366)	
Credit Program Receivables	5		384,284	
Credit Program Receivables	6		(23,287)	
Credit Program Receivables	11		53,901	
Credit Program Receivables	13		(316,063)	
Total Credit Program Receivables		**5,469,485**	**(872,531)**	**$4,596,954**
Advances - Public	5		(379,856)	
Advances - Public	6		23,287	
Total Advances - Public		**379,856**	**(356,569)**	**23,287**
Accounts Payable - Intragovernmental Liabilities	1	27,992	(3,107)	24,885
Debt	1	11,138,280	3,104	11,141,384
Other Liabilities - Intragovernmental Liabilities	1		151,198	
Other Liabilities - Intragovernmental Liabilities	3		107,508	
Other Liabilities - Intragovernmental Liabilities	11		13,768	
Total Other Liabilities - Intragovernmental Liabilities		**947,039**	**272,474**	**1,219,513**
Accounts Payable - Public	12	149,134	(21,327)	127,807
Liabilities for Loan Guarantees - Public	2		123,452	
Liabilities for Loan Guarantees - Public	3		(107,508)	
Liabilities for Loan Guarantees - Public	11		(4,652)	
Liabilities for Loan Guarantees - Public	12		21,328	
Liabilities for Loan Guarantees - Public	13		(316,065)	
Total - Liabilities for Loan Guarantees - Public		**1,525,038**	**(283,445)**	**1,241,593**
Other - Public	4		16,531	
Other - Public	9		39,700	
Other - Public	11		44,786	
Total Other - Public		**56,416**	**101,017**	**157,433**
Unexpended Appropriations	4		(16,150)	
Unexpended Appropriations	9		(39,700)	
Total Unexpended Appropriations		**1,010,485**	**(55,850)**	**954,635**
Cumulative Results of Operations	1		(1,122,938)	
Cumulative Results of Operations	2		(123,452)	
Cumulative Results of Operations	4		(28,165)	
Cumulative Results of Operations	5		5,707	
Cumulative Results of Operations	9		22,459	
Total Cumulative Results of Operations		**(1,451,573)**	**(1,246,389)**	**(2,697,962)**

Statement of Net Cost

Champion Small Business Interests			
Intragovernmental Gross Costs		3,453	3,453
Intragovernmental Net Costs		3,453	3,453
Gross Costs with the Public		14,576	
Gross Costs with the Public	9	156	
Total Gross Costs with the Public		**14,732**	**14,732**
Net Costs with the Public		14,576	
Net Costs with the Public	9	156	
Total Net Costs with the Public		**14,732**	**14,732**
Net Cost of Champion Small Business Interests		18,029	
Net Cost of Champion Small Business Interests	9	156	
Total Net Cost of Champion Small Business Interests		**18,185**	**18,185**
Empowering Entrepreneurs			
Intragovernmental Gross Costs		(8,004)	(8,004)
Less: Intragovernmental Earned Revenue		32,148	32,148
Intragovernmental Net Costs		(40,152)	(40,152)
Gross Costs with the Public		989,941	
Gross Costs with the Public	2	123,452	
Gross Costs with the Public	3	(5,153)	
Gross Costs with the Public	9	(6,138)	
Gross Costs with the Public	11	(36,728)	
Gross Costs with the Public	12	47,972	
Total Gross Costs with the Public		**1,113,346**	**1,113,346**
Less: Earned Revenue from the Public		177,379	
Less: Earned Revenue from the Public	11	(36,728)	
Less: Earned Revenue from the Public	12	47,925	
Total Less: Earned Revenue from the Public		**188,576**	**188,576**
Net Costs with the Public		812,562	
Net Costs with the Public	2	123,452	
Net Costs with the Public	3	(5,153)	
Net Costs with the Public	9	(6,138)	
Net Costs with the Public	12	47	
Total Net Costs with the Public		**924,770**	**924,770**
Net Cost of Champion Small Business Interests		772,410	
Net Cost of Champion Small Business Interests	2	123,452	
Net Cost of Champion Small Business Interests	3	(5,153)	
Net Cost of Champion Small Business Interests	9	(6,138)	
Net Cost of Champion Small Business Interests	12	47	
Total Net Cost of Champion Small Business Interests		**884,618**	**884,618**

Business Programs

Intragovernmental Gross Costs		(4,551)	4,551	
Less: Intragovernmental Earned Revenue		32,148	(32,148)	
Intragovernmental Net Costs		(36,699)	36,699	
Gross Costs with the Public		1,004,517	(1,004,517)	
Less: Earned Revenue from the Public		177,379	(177,379)	
Net Costs with the Public		**827,138**	**(827,138)**	
Net Cost of Business Programs		**790,439**	**(790,439)**	

Disaster Assistance Programs

Intragovernmental Gross Costs	4	684,009	(1)	684,008
Intragovernmental Net Costs	4	248,130	(1)	248,129
Gross Costs with the Public	1		321,410	321,410
Gross Costs with the Public	9		2,285	2,285
Total Gross Costs with the Public		**330,940**	**323,695**	**654,635**
Less: Earned Revenue from the Public	11	257,708	551	258,259
Net Costs with the Public	1		321,410	
Net Costs with the Public	9		2,285	
Net Costs with the Public	11		(551)	
Total Net Costs with the Public		**73,232**	**323,144**	**396,376**
Net Cost of Disaster Assistance Programs	1		321,410	
Net Cost of Disaster Assistance Programs	9		2,284	
Net Cost of Disaster Assistance Programs	11		(551)	
Total Net Cost of Disaster Assistance Programs		**321,362**	**323,143**	**644,505**
Costs Not Assigned to Programs	9	40,410	636	41,046
Less: Earned Revenue not attributed to Programs	4	16,752	(17,037)	(285)
Net Cost not assigned to Programs	4		17,037	
Net Cost not assigned to Programs	9		636	
Total Net Cost not assigned to Programs		**23,658**	**17,673**	**41,331**
Net Cost of Operations	1		321,410	
Net Cost of Operations	2		123,452	
Net Cost of Operations	3		(5,153)	
Net Cost of Operations	4		17,037	
Net Cost of Operations	9		(3,062)	
Net Cost of Operations	11		(551)	
Net Cost of Operations	12		47	
Total Net Cost of Operations		1,135,459	453,180	1,588,639

Statement of Changes in Net Position

Prior Period Adjustments	1		$(801,530)	
Prior Period Adjustments	4		$(1,825)	
Prior Period Adjustments	9		(29,500)	
Total Prior Period Adjustments		**557**	**(832,855)**	**(832,298)**
Other Adjustments	4	(2,643)	2,709	66

Appropriations Used - Cumulative Results of Operations	5		16,157	
Appropriations Used - Cumulative Results of Operations	9		33,610	
Total Appropriations Used - Cumulative Results of Operations		**1,014,898**	**49,767**	**1,064,665**
Appropriations Used - Unexpended Appropriations	5		(39,567)	
Appropriations Used - Unexpended Appropriations	9		(10,200)	
Total Appropriations Used - Unexpended Appropriations		(1,014,898)	(49,767)	(1,064,665)
Other - Current Year Liquidating Equity Activity (+/-)	3		(5,151)	
Other - Current Year Liquidating Equity Activity (+/-)	11		(13,768)	
Total Other - Current Year Liquidating Equity Activity (+/-)		**(204,976)**	**(18,919)**	**(223,895)**

Statement of Budgetary Resources

Unobligated Balance Brought Forward October 1	12	$7,443,010	$17,109	7,460,119
Spending Authority from Offsetting Collections				
Earned	4		(6,958)	
Earned	10		29,545	
Total Earned		**2,961,112**	**22,587**	**2,983,699**
Change in Unfilled Customer Orders	4	195,987	6,174	202,161
Recoveries of Prior Year Obligations	7	266,595	20,633	287,228
Obligations Incurred	4		(951)	
Obligations Incurred	7		16,405	
Obligations Incurred	10		29,545	
Total Obligations Incurred		**5,084,400**	**44,999**	**5,129,399**
Unobligated Balances Available	12	3,045,798	4,228	3,050,026
Unobligated Balances Not Available	4		167	
Unobligated Balances Not Available	12		17,100	
Total Unobligated Balances Not Available		**3,694,382**	**17,267**	**3,711,649**
Obligated Balance, Beginning of Period	12	1,177,283	(17,101)	1,160,182
Accounts Receivable	4	(72,611)	(167)	(72,778)
Undelivered Orders	9	707,651	(39,700)	667,951
Accounts Payable	9		39,700	
Accounts Payable	12		(21,328)	
Total Accounts Payable		**258,327**	**18,372**	**276,699**
Total Obligated Balance, End of Period		**752,454**	**(21,495)**	**730,959**
Disbursements	4		(951)	
Disbursements	10		29,545	
Total Disbursements		**5,631,546**	**28,594**	**5,660,140**
Collections	4		952	
Collections	10		(29,545)	
Total Collections		**(3,546,014)**	**(28,593)**	**(3,574,607)**

Statement of Financing

Obligations Incurred	4		$(951)	
Obligations Incurred	7		16,405	
Obligations Incurred	10		29,545	
Total Obligations Incurred		**$5,084,400**	**44,999**	**$5,129,399**
Spending Authority from Offsetting Collections and Recoveries	4		(784)	
Spending Authority from Offsetting Collections and Recoveries	7		16,405	
Spending Authority from Offsetting Collections and Recoveries	10		29,545	
Spending Authority from Offsetting Collections and Recoveries	12		4,228	
Total Spending Authority from Offsetting Collections and Recoveries		**3,423,694**	**49,394**	**3,473,088**
Obligations Net of Offsetting Collections and Recoveries	4		(167)	
Obligations Net of Offsetting Collections and Recoveries	12		(4,228)	
Total Obligations Net of Offsetting Collections and Recoveries		**1,660,706**	**(4,395)**	**1,656,311**
Other Financing Sources	3		(5,151)	
Other Financing Sources	11		(13,768)	
Total Other Financing Sources		**(204,976)**	**(18,919)**	**(223,895)**
Net Other Resources Used to Finance Activities	3		(5,151)	
Net Other Resources Used to Finance Activities	11		(13,768)	
Total Net Other Resources Used to Finance Activities		**(450,683)**	**(18,919)**	**(469,602)**
Change in Undelivered Orders	4		45,736	
Change in Undelivered Orders	9		10,200	
Total Change in Undelivered Orders		**270,531**	**55,936**	**326,467**
Resources that Finance the Acquisition of Assets or Liquidation of Liabilities	6	(3,070,232)	(189,470)	(3,259,702)
Adjustments to Net Obligated Resources That Do Not Affect Net Cost of Operations	4	9,085	(15,340)	(6,255)
Upward / Downward reestimates of Credit Subsidy Expense	1		321,410	
Upward / Downward reestimates of Credit Subsidy Expense	2		123,451	
Total Upward / Downward reestimates of Credit Subsidy Expense		**542,065**	**444,861**	**986,926**
Change in Revenue Receivable from Public	11	64,399	(13,767)	50,632
Change in Due to Treasury - Liquidating Funds That is not an Obligation	3		5,153	
Change in Due to Treasury - Liquidating Funds That is not an Obligation	11		13,768	
Total Change in Due to Treasury - Liquidating Funds That is not an Obligation		**204,976**	**18,921**	**223,897**
Provision for Losses on Estimated Guarantees	3	(242,945)	(5,153)	(248,098)
Bad Debt Expense - Noncredit Reform	6	14,153	180,506	194,659

REQUIRED SUPPLEMENTARY STEWARDSHIP INFORMATION

Required Supplementary Stewardship Information
Stewardship Investments in Human Capital

for the periods ended September 30, 2003, 2002, 2001, 2000 and 1999

(DOLLARS IN THOUSANDS)

	2003	2002	2001	2000	1999
Office of Small Business Development Centers	$99,293	$100,276	$98,583	$88,162	$79,078
Office of Women's Business Ownership	15,361	16,141	15,934	6,488	12,085
Other Business Initiatives	12,639	12,057	6,050	4,900	4,254
Counseling & Training	12,315				
Service Corps of Retired Executives	10,305	15,021	5,988	8,210	9,236
Business Information Centers	8,426	14,033	16,015	11,719	7,832
US Exports Assistance Center	3,500	2,174			
CoSponsorships	1,102				
Electronic Government	259	659			
National Education Center	259				
Office of Native American Affairs	194	856	1,394	1,748	2,504
Disability Initiative	65	132	8		
BATF donations - Reimbursed Expenses	65	66			
One Stop Capital Shops			8,114	8,495	5,137
Business Linc			2,518		
Welfare to Work			8	2,034	2,988
Office of International Trade			2,955		5,769
Egypt, Nigeria - Reimbursed Expenses					
Office of Veterans' Affairs(1)				2,776	2,862
Ombudsman(1)				1,507	3,396
Women's Business Council (1)				1,106	693
HubZones Program (1)				6,734	4,872
Small Business Innovation and Research (1)					3,597
Total	**$163,783**	**$161,415**	**$157,567**	**$143,879**	**$144,303**

(1) Office of Veterans' Affairs, Ombudsman, and Women's Business Council are now reported under "Improving Business Environment". **HubZones Program** is currently reported under "Business Development". **Small Business Innovation and Research** is reported under "Government Contracting".

Human Capital. Human Capital investments are expenses included in net cost for education and training programs that are intended to increase or maintain national economic productive capacity and that produce outputs and outcomes that provide evidence of maintaining or increasing national productive capacity. The definition excludes education and training expenses for Federal personnel.

A description of the major programs, outputs, and outcomes may be found in this Performance and Accountability Report.

Office of Small Business Development Centers delivers management and technical assistance, economic development and management training to existing and prospective small businesses through cooperative agreements with universities and colleges and government organizations.

Office of Women's Business Ownership provides assistance to women business owners and acts as their advocate in the public and private sectors. This program includes the operation of Women's Business Centers that provide assistance to women entrepreneurs in a number of locations around the U.S.

Other Business Initiatives include Youth Entrepreneurship, Classroom and e-commerce, and PRIME. E-commerce provide assistance to small business through the provision of information and SBA program access through the internet and other electronic access.

Counseling and Training is a new category of SBA service in FY 2003 that provides assistance to small business in SBA field offices in counseling and training activities.

Service Corps of Retired Executives is a nonprofit organization which provides small business counseling and training under a grant from the U.S. Small Business Administration (SBA). SCORE members are successful, retired business men and women who volunteer their time to assist aspiring entrepreneurs and small business owners. There are SCORE chapters in every state.

Business Information Centers (BICs) provide a one-stop location where current and future small business owners can receive assistance and advice. Through partnerships with the public and private sector, BICs offer the latest computer technology, hardware and software, as well as extensive small business reference library of hard copy books and publications and current management videotapes for entrepreneurs. At a BIC they can plan their business, expand an existing business, or venture into new business areas. The use of software for a variety of business applications offers clients of all types a means for addressing diverse needs.

US Export Assistance Centers provide assistance to small business entrepreneurs in the form of advice on how to conduct business activities to export goods and services. This is a new category in FY 2003.

CoSponsorships was added as a category in FY 2003 to include the educational assistance provided to small business by SBA in partnership with non government organizations.

Electronic Government was added as a category in FY 2003 for services provided to small business through electronic processing activity and electronic information.

National Education Center is a new activity in FY 2003 that provides a forum for the education of small business people from a centralized location in Florida.

Office of Native American Affairs provides assistance to American Indian, Native Alaskan, and Native Hawaiian small business clients, tribally owned small businesses, and small businesses located in Native American communities.

Disability Initiative The SBA is helping small businesses gain access to a new pool of potential workers as well as assisting Americans with disabilities start small businesses.

BATF donations are used by SBA to provide assistance to small business in the form of educational services.

One Stop Capital Shops combines SBA resources and community partnerships to offer entrepreneurial development assistance to small businesses located in distressed inner cities and rural communities. SBA funding for this program was discontinued in FY 2002.

Business Linc On June 5, 1998 the BusinessLINC initiative was announced to encourage more private sector business-to-business linkages that enhance the economic vitality and competitive capacity of small businesses, particularly those located in economically distressed urban and rural areas. This program was improperly categorized as Human Capital enhancement in FY 2001.

Welfare to Work The SBA helped small businesses gain access to a new pool of potential workers as well as helping former welfare recipients become entrepreneurs. This program ended effectively in FY 2000.

Office of International Trade provides assistance to small businesses obtain financing for export activity. This activity was improperly reported as a stewardship investment in human capital for several years in the past.

Egypt and Nigeria reimbursed expenses helped to fund activities to promote small business development in these countries. They were incorrectly reported as investment in human capital in the past.

Required Supplementary Stewardship Information
Stewardship Investments in Research and Development
for the periods ended September 30, 2003, 2002, 2001, 2000 and1999

(DOLLARS IN THOUSANDS)

	2003	2002	2001	2000	1999
The Office of Technology	$778	$1,103	$1,906	$1,720	$3,597

Research and Development. Research and Development investments are expenses included in net cost incurred to support the search for new or refined knowledge and ideas and for the application or use of such knowledge and ideas for the development of new or improved products and processes with the expectation of maintaining or increasing national economic productive capacity or yielding other future benefits.

A detailed description of the programs, outputs, and outcomes may be found in the Government Performance and Results Act (GPRA) Details portion of the Performance and Accountability Report.

REQUIRED SUPPLEMENTAL INFORMATION

Required Supplementary Information
Intragovernmental Assets and Liabilities
for the period ended September 30, 2003

(DOLLARS IN THOUSANDS)

Trading Partner	Fund Balance With Treasury	Accounts Receivable	Accounts Payable	Debt/Borrowings from Other Agencies	Other Liabilities
Department of Defense					
Federal Financing Bank			$4,634	$79,630	$1,855
Agency for International Development					210
Department of Labor					5,708
Office of Personnel Management					
Department of the Treasury	2,798,677	12,650	9,083	6,626,749	796,003
Other Agencies			20		36,620
Total	**$2,798,677**	**$12,650**	**$13,737**	**$6,706,379**	**$840,396**

Required Supplementary Information
Intragovernmental Earned Revenues and Related Costs
for the period ended September 30, 2003

(DOLLARS IN THOUSANDS)

Trading Partner	Earned Revenue	Gross Cost
Department of the Treasury	$335,059	$641,363
Total	**$335,059**	**$641,363**
Budget Functional Classification		
Commerce and Housing Credit	$53,335	$504,444
Community and Regional Development	281,724	136,919
Total	**$335,059**	**$641,363**

The Intragovernmental Earned Revenues and Related Costs are for the SBA's Financing Accounts; therefore interest earned is an offset to cost of operations.

Required Supplementary Information
Combining Statement of Budgetary Resources
for the period ended September 30, 2003

(DOLLARS IN THOUSANDS)

	BLIF		DLF		SBGRF
	Budgetary	Non-Budgetary Financing	Budgetary	Non-Budgetary Financing	Budgetary
BUDGETARY RESOURCES					
Budget Authority					
Appropriations Received	$938,710	$	$659,319	$	$
Borrowing Authority		327,029		831,167	
Net Transfers (+/-)			(500)		
Other					
Unobligated Balance					
Brought Forward October 1	421,979	564,230	185,309	5,485,630	25,600
Net Transfers (+/-)			(9,000)		
Spending Authority from Offsetting Collections					
Earned	164,413	1,424,107	62,098	1,539,510	5,868
Change in Unfilled Customer Orders		(11,159)		(1,771)	
Anticipated					
Recoveries of Prior Year Obligations	78,161	2,215	25,003	83,400	
Anticipated					
Temporarily Not Available Pursuant to					
Public Law					
Permanently Not Available	(321,912)	(74,852)	(114,094)	(5,492,457)	1
Anticipated					
Total Budgetary Resources	**$1,281,351**	**$2,231,570**	**$808,135**	**$2,445,479**	**$31,469**

Required Supplementary Information
Combining Statement of Budgetary Resources
for the period ended September 30, 2003

(DOLLARS IN THOUSANDS)

	BLIF		DLF		SBGRF
STATUS OF BUDGETARY RESOURCES	**Budgetary**	**Non-Budgetary Financing**	**Budgetary**	**Non-Budgetary Financing**	**Budgetary**
Obligations Incurred	$1,024,438	$1,667,479	$710,919	$1,240,368	$8,828
Unobligated Balances Available					
Apportioned - Currently Available	224,492	235,785	27,754	1,000,911	22,161
Anticipated					
Exempt from Apportionment					
Unobligated Balances					
Not Yet Available	32,421	328,306	69,462	204,200	480
Total Status of Budgetary Resources	**$1,281,351**	**$2,231,570**	**$808,135**	**$2,445,479**	**$31,469**

	BLIF		DLF		SBGRF
RELATIONSHIP OF OBLIGATIONS TO OUTLAYS	**Budgetary**	**Non-Budgetary Financing**	**Budgetary**	**Non-Budgetary Financing**	**Budgetary**
Obligated Balance,					
Beginning of Period	$180,031	$21,030	$48,224	$186,060	$1,106
Obligated Balance, End of Period					
Accounts Receivable	(3,174)	(18,308)	(90)	(16,554)	
Unfilled Customer Orders from Federal Sources		(91,618)		(36,365)	
Undelivered Orders	84,969	31,454	36,407	229,599	
Accounts Payable	38,905	38,216	3,866	3,407	337
Total Obligated Balance, End of Period	**120,700**	**(40,256)**	**40,183**	**180,087**	**337**
Outlays					
Disbursements	1,006,901	1,724,604	705,988	1,198,977	9,596
Collections	(165,708)	(1,411,000)	(74,131)	(1,573,774)	-5,868
Subtotal	**$841,193**	**$313,604**	**$631,857**	**($374,797)**	**$3,728**
Less: Offsetting Receipts		258,107		41,712	
Net Outlays	**$841,193**	**$55,497**	**$631,857**	**($416,509)**	**$3,728**

Required Supplementary Information
Combining Statement of Budgetary Resources
for the period ended September 30, 2003

(DOLLARS IN THOUSANDS)

	PCECGF	SE	OIG	BATF	TOTAL	TOTAL	
	Budgetary	Budgetary	Budgetary	Budgetary	Budgetary	Non-Budgetary Financing	Total
BUDGETARY RESOURCES							
Budget Authority							
Appropriations Received	$3,000	$369,457	$12,422	$	$1,982,908	$	$1,982,908
Borrowing Authority						1,158,196	1,158,196
Net Transfers (+/-)		500					
Other							
Unobligated Balance:							
Brought Forward October 1	3,208	74,954	608	263	711,921	6,049,860	6,761,781
Net Transfers (+/-)					(9,000)		(9,000)
Spending Authority from Offsetting Collections							
Earned	264	253,834	547	208	487,232	2,963,617	3,450,849
Change in Unfilled Customer Orders		(9,022)	124		(8,898)	(12,930)	(21,828)
Anticipated							
Recoveries of Prior Year Obligations		22,501	247	2	125,914	85,615	211,529
Anticipated							
Temporarily Not Available Pursuant to							
Public Law							
Permanently Not Available	(3,208)	(22,050)	(149)		(461,412)	(5,567,309)	(6,028,721)
Anticipated							
Total Budgetary Resources	**$3,264**	**$690,174**	**$13,799**	**$473**	**$2,828,665**	**$4,677,049**	**$7,505,714**

Required Supplementary Information
Combining Statement of Budgetary Resources
for the period ended September 30, 2003

(DOLLARS IN THOUSANDS)

	PCECGF	SE	OIG	BATF	TOTAL	TOTAL	
STATUS OF BUDGETARY RESOURCES	**Budgetary**	**Budgetary**	**Budgetary**	**Budgetary**	**Budgetary**	**Non-Budgetary Financing**	**Total**
Obligations Incurred	$2	$655,589	$13,137	$55	$668,783	$	$668,783
Unobligated Balances Available							
Apportioned - Currently Available	3,262	9,365	245	48	12,920		12,920
Anticipated							
Exempt from Apportionment				357	357		357
Unobligated Balances							
Not Yet Available		25,220	417	13	25,650		25,650
Total Status of Budgetary Resources	**$3,264**	**$690,174**	**$13,799**	**$473**	**$707,710**	**$**	**$707,710**

	PCECGF	SE	OIG	BATF	TOTAL	TOTAL	
RELATIONSHIP OFOBLIGATIONS TO OUTLAYS	**Budgetary**	**Budgetary**	**Budgetary**	**Budgetary**	**Budgetary**	**Non-Budgetary Financing**	**Total**
Obligated Balance,							
Beginning of Period	$	$293,604	$889	$15	$294,508	$	$294,508
Obligated Balance - End of Period							
Accounts Receivable							
Unfilled Customer Orders from							
Federal Sources		(233)			(233)		(233)
Undelivered Orders		260,085	1,405	21	261,511		261,511
Accounts Payable		51,207	234		51,441		51,441
Total Obligated Balance, End of Period		**311,059**	**1,639**	**21**	**312,719**		**312,719**
Outlays:							
Disbursements	2	615,567	12,141	46	627,756		627,756
Collections	(264)	(244,746)	(671)	(208)	(245,889)		(245,889)
Subtotal	**$(262)**	**$370,821**	**$11,470**	**$(162)**	**$381,868**	**$**	**$381,868**
Less: Offsetting Receipts							
Net Outlays	**$(262)**	**$370,821**	**$11,470**	**$(162)**	**$381,868**	**$**	**$381,868**

Additional Accompanying Information
Consolidating Balance Sheet
for the period ended September 30, 2003

(DOLLARS IN THOUSANDS)

ASSETS	BLIF	DLF	SBGRF	PCECGF	SE	OIG	BATF	Combined Total
Intragovernmental Assets								
Fund Balances with Treasury	$901,448	$1,522,597	$22,978	$3,262	$345,651	$2,301	$440	$2,798,677
Accounts Receivable	2,417,106	1,316,475			1,688			3,735,269
Advances	4,229	45,247						49,476
Total Intragovernmental	$3,322,783	$2,884,319	$22,978	$3,262	$347,339	$2,301	$440	$6,583,422
Assets - Public and Other								
Cash	5,331							5,331
Accounts Receivable	29,478	36	5,877		81			35,472
Credit Program Receivables and Related								
Foreclosed Property, Net	1,662,657	2,621,608		16,068				4,300,333
General Property and Equipment, Net					8,522			8,522
Advances and Other Assets								
Total Assets - Public and Other	1,697,466	2,621,644	5,877	16,068	8,603	0	0	4,349,658
Total Assets	**$5,020,249**	**$5,505,963**	**$28,855**	**$19,330**	**$355,942**	**$2,301**	**$440**	**$10,933,080**

Additional Accompanying Information
Consolidating Balance Sheet
for the period ended September 30, 2003

(DOLLARS IN THOUSANDS)

LIABILITIES	BLIF	DLF	SBGRF	PCECGF	SE	OIG	BATF	Combined Total
Intragovernmental Liabilities								
Accounts Payable	$2,433,072	$1,302,814	$	$	$470	$	$	$3,736,356
Debt	1,625,476	5,080,903						6,706,379
Other	525,213	288,004		19,330	57,139	186		889,872
Total Intragovernmental	$4,583,761	$6,671,721	$0	$19,330	$57,609	$186	$0	$11,332,607
Other Liabilities -Public								
Accounts Payable	$39,357	$8,801	$346	$	$1,144	$	$	$49,648
Liabilities for Loan Guarantees	2,548,963							2,548,963
FECA Actuarial Liability					31,822			31,822
Other	40,915	5,606	19,718		73,824	225		140,288
Total Other Liabilities -Public	2,629,235	14,407	20,064	0	106,790	225	0	2,770,721
Total Liabilities	**$7,212,996**	**$6,686,128**	**$20,064**	**$19,330**	**$164,399**	**$411**	**$0**	**$14,103,328**
NET POSITION								
Unexpended Appropriations	$202,882	$119,271	$280,872	$	$242,033	$2,416	$	$847,474
Cumulative Results of Operations	(2,395,629)	(1,299,436)	(272,081)		(50,490)	(526)	440	(4,017,722)
Total Net Position	**$(2,192,747)**	**$(1,180,165)**	**$8,791**	**$0**	**$191,543**	**$1,890**	**$440**	**$(3,170,248)**
Total Liabilities and Net Position	**$5,020,249**	**$5,505,963**	**$28,855**	**$19,330**	**$355,942**	**$2,301**	**$440**	**$10,933,080**

Additional Accompanying Information
Consolidating Balance Sheet
for the period ended September 30, 2003

(DOLLARS IN THOUSANDS)

ASSETS	Eliminations	Consolidated TOTAL
Intragovernmental Assets		
Fund Balances with Treasury	$	$2,798,677
Accounts Receivable	(3,722,619)	12,650
Advances	(49,476)	
Total Intragovernmental	$(3,772,095)	$2,811,327
Other Assets -Public		
Cash		5,331
Accounts Receivable		35,472
Credit Program Receivables and Related		
Foreclosed Property, Net		4,300,333
General Property and Equipment, Net		8,522
Advances		
Total Other Assets -Public	0	4,349,658
Total Assets	**$(3,772,095)**	**$7,160,985**

Additional Accompanying Information
Consolidating Balance Sheet
for the period ended September 30, 2003

(DOLLARS IN THOUSANDS)

LIABILITIES		
Intragovernmental Liabilities		
Accounts Payable	$(3,722,619)	$13,737
Debt		6,706,379
Other	(49,476)	840,396
Total Intragovernmental	$(3,772,095)	$7,560,512
Other Liabilities -Public		
Accounts Payable	$	49,648
Liabilities for Loan Guarantees		2,548,963
FECA Actuarial Liability		31,822
Other		140,288
Total Other Liabilities -Public	0	2,770,721
Total Liabilities	**$(3,772,095)**	**$10,331,233**
NET POSITION		
Unexpended Appropriations	$	847,474
Cumulative Results of Operations		(4,017,722)
Total Net Position	**$0**	**$(3,170,248)**
Total Liabilities and Net Position	**$(3,772,095)**	**$7,160,985**

Additional Accompanying Information
Consolidating Statement of Financing
for the period ended September 30, 2003

(DOLLARS IN THOUSANDS)

Resources Used to Finance Activities	BLIF	DLF	SBGRF	PCECGF	SE	OIG	BATF	Total
Budgetary Resources								
Obligated								
Obligations Incurred	$2,691,917	$1,951,287	$8,828	$2	$655,589	$13,137	$55	$5,320,815
Less: Spending Authority from								
Offsetting Collections and Recoveries	1,657,737	1,708,240	5,868	264	267,313	918	210	3,640,550
Obligations Net of Offsetting								
Collections and Recoveries	1,034,180	243,047	2,960	(262)	388,276	12,219	(155)	1,680,265
Less: Offsetting Receipts	258,107	41,712						299,819
Net Obligations	**$776,073**	**$201,335**	**$2,960**	**$(262)**	**$388,276**	**$12,219**	**$(155)**	**$1,380,446**
Other Resources								
Transfers In (Out)	(173,403)	(2,205)						(175,608)
Imputed Financing					19,063			19,063
Other Financing Sources	(7,009)	407		(276)				(6,878)
Net Other Resources Used to Finance Activities	**$(180,412)**	**$(1,798)**	**$0**	**$(276)**	**$19,063**	**$0**	**$0**	**$(163,423)**
Total Resources Used to Finance Activities	**$595,661**	**$199,537**	**$2,960**	**$(538)**	**$407,339**	**$12,219**	**$(155)**	**$1,217,023**

Additional Accompanying Information
Consolidating Statement of Financing
for the period ended September 30, 2003

(DOLLARS IN THOUSANDS)

Resources Used to Finance	BLIF	DLF	SBGRF	PCECGF	SE	OIG	BATF	Total
Items not Part of the Net Cost of Operations								
Change in Amount of Goods, Services and Benefits Ordered But Not Yet Provided	$44,406	$(9,922)	$	$	$(21,909)	$(544)	$(6)	$12,025
Budgetary Offsetting Collections and Receipts that Do Not Affect Net Cost of Operations	1,424,107	1,539,510						2,963,617
Resources that Finance the Acquisition of Assets or Liquidation of Liabilities	(1,338,000)	(1,049,620)		200	(4,713)			(2,392,133)
Other Resources or Adjustments to Net Obligated Resources That Do Not Affect Net Cost of Operations	2,004	227	24	1	(1,030)	(113)	207	1,320
Total Resources Used to Finance Items Not Part of the Net Cost of Operations	**$132,517**	**$480,195**	**$24**	**$201**	**$(27,652)**	**$(657)**	**$201**	**$584,829**
Total Resources Used to Finance the Net Cost of Operations	**$728,178**	**$679,732**	**$2,984**	**$(337)**	**$379,687**	**$11,562**	**$46**	**$1,801,852**

Additional Accompanying Information
Consolidating Statement of Financing
for the period ended September 30, 2003

(DOLLARS IN THOUSANDS)

	BLIF	DLF	SBGRF	PCECGF	SE	OIG	BATF	Total
Components of the Net Cost of Operations that will not Require or Generate Resources in the Current Period								
Change in Annual Leave Liability					650			650
Increase in Unfunded Liability for Claims against SBA								
Upward/ Downward reestimates of Credit Subsidy Expense	1,604,191	(284,604)						1,319,587
Change in Revenue Receivable from Public	6,848	1,334	(736)	(19)	508	28		7,963
Change in Due to Treasury - Liquidating Funds that is not an obligation	7,011	(407)		276				6,880
Provision for Losses on Estimated Guarantees	5,464		4,628					10,092
Unfunded Employee Benefits					671			671
Components of the Net Cost of Operations that will not Require or Generate Resources in the Current Period	**$1,623,514**	**$(283,677)**	**$3,892**	**$257**	**$1,829**	**$28**	**$0**	**$1,345,843**
Components Not Requiring or Generating Resources								
Depreciation or Amortization					3,018			3,018
Bad Debt Expense - Noncredit Reform	17,648	3,681		(196)	(165)			20,968
Total Components of Net Cost that Will Not Require or Generate Resources	**17,648**	**3,681**		**(196)**	**2,853**			**23,986**
Total Components of NetCost of Operations Not Requiring or Generating Resources in the Current Period	**$1,641,162**	**$(279,996)**	**$3,892**	**$61**	**$4,682**	**$28**	**$0**	**$1,369,829**
Net Cost of Operations	**$2,369,340**	**$399,736**	**$6,876**	**$(276)**	**$384,369**	**$11,590**	**$46**	**$3,171,681**

Consolidating Statement of Changes in Net Position for the period ended September 30, 2003

(DOLLARS IN THOUSANDS)

	BLIF		DLF		SBGRF	
	Cumulative Results of Operations	Unexpended Appropriations	Cumulative Results of Operations	Unexpended Appropriations	Cumulative Results of Operations	Unexpended Appropriations
Beginning Balances	$ (791,440)	$249,236	$(1,584,040)	$156,834	$(273,334)	$289,001
Prior Period Adjustments						
Beginning Balances, as Adjusted	**(791,440)**	**249,236**	**(1,584,040)**	**156,834**	**(273,334)**	**289,001**
Budgetary Financing Sources						
Appropriations Received		938,710		659,319		
Appropriations						
Transferred -in/out (+/-)				(9,500)		
Rescissions		(11,893)		(1,244)		
Adjustment - Cancelled						
Authority		(13)				
Other Adjustments		(27,595)				
Appropriations Used	945,563	(945,563)	686,138	(686,138)	8,129	(8,129)
Donations of Cash						
Transfers-in/out Without						
Reimbursement						

Consolidating Statement of Changes in Net Position for the period ended September 30, 2003

(DOLLARS IN THOUSANDS)

	BLIF		DLF		SBGRF	
	Cumulative Results of Operations	Unexpended Appropriations	Cumulative Results of Operations	Unexpended Appropriations	Cumulative Results of Operations	Unexpended Appropriations
Other Financing Sources						
Transfers-in/out Without Reimbursement	(173,403)		(2,205)			
Imputed Financing from Costs Absorbed by Others						
Other - Current Year Liquidating Equity Activity (+/-)	(7,009)		407			
Total Financing Sources	**$765,151**	**$(46,354)**	**$684,340**	**$(37,563)**	**$8,129**	**$(8,129)**
Less: Net Cost of Operations	**$2,369,340**		**$399,736**		**$6,876**	
Net Position - End of Period	**$(2,395,629)**	**$202,882**	**$(1,299,436)**	**$119,271**	**$(272,081)**	**$280,872**

On the Consolidated Statement of Net Costs, the costs are reported by major program using the SBA's cost accounting study, while on this statement the costs are reported by fund and are not allocated using the cost accounting study.

Additional Accompanying Information
Consolidating Statement of Changes in Net Position
for the period ended September 30, 2003

(DOLLARS IN THOUSANDS)

	PCECGF		SE		OIG	
	Cumulative Results of Operations	Unexpended Appropriations	Cumulative Results of Operations	Unexpended Appropriations	Cumulative Results of Operations	Unexpended Appropriations
Beginning Balances	$0	$0	$(48,905)	$257,834	$(524)	41,728
Prior Period Adjustments						
Beginning Balances, as Adjusted	**0**	**0**	**(48,905)**	**257,834**	**(524)**	**1,728**
Budgetary Financing Sources						
Appropriations Received		3,000		369,457		12,422
Appropriations						
Transferred -in/out (+/-)				500		
Rescissions				(16,152)		(80)
Adjustment -Cancelled						
Authority				(5,899)		(66)
Other Adjustments		(3,000)		14		
Appropriations Used			363,721	(363,721)	11,588	(11,588)
Donations of Cash						
Transfers-in/out Without						
Reimbursement						
Other Financing Sources						
Transfers-in/out Without						
Reimbursement						
Imputed Financing from						
Costs Absorbed by Others			19,063			

Additional Accompanying Information
Consolidating Statement of Changes in Net Position
for the period ended September 30, 2003

(DOLLARS IN THOUSANDS)

	PCECGF		SE		OIG	
	Cumulative Results of Operations	Unexpended Appropriations	Cumulative Results of Operations	Unexpended Appropriations	Cumulative Results of Operations	Unexpended Appropriations
Other - Current Year						
Liquidating Equity Activity (+/-)	(276)					
Total Financing Sources	**$(276)**	**$0**	**$382,784**	**$(15,801)**	**$11,588**	**$688**
Less: Net Cost of Operations	**$((276)**		**$384,369**		**$11,590**	
Net Position - End of Period	**$0**	**$0**	**$(50,490)**	**$242,033**	**$(526)**	**2,416**

On the Consolidated Statement of Net Costs, the costs are reported by major program using the SBA's cost accounting study, while on this statement the costs are reported by fund and are not allocated using the cost accounting study.

Additional Accompanying Information
Consolidating Statement of Changes in Net Position
for the period ended September 30, 2003

(DOLLARS IN THOUSANDS)

	BATF		Eliminations		TOTAL		
	Cumulative Results of Operations	Unexpended Appropriations	Cumulative Results of Operations	Unexpended Appropriations	Cumulative Results of Operations	Unexpended Appropriations	Total
Beginning Balances	$279	$0	$0	$0	$(2,697,964)	$954,633	$(1,743,331)
Prior Period Adjustments						$0	
Beginning Balances, as Adjusted	**279**	**0**	**0**	**0**	**(2,697,964)**	**954,633**	**(1,743,331)**
Budgetary Financing Sources							
Appropriations Received						1,982,908	1,982,908
Appropriations							
Transferred -in/out (+/-)						(9,000)	(9,000)
Rescissions						(29,369)	(29,369)
Adjustment -Cancelled							
Authority						(5,978)	(5,978)
Other Adjustments						(30,581)	(30,581)
Appropriations Used					2,015,139	(2,015,139)	
Donations of Cash	207				207		207
Transfers-in/out Without							
Reimbursement							
Other Financing Sources							
Transfers-in/out Without							
Reimbursement					(175,608)		(175,608)
Imputed Financing from							
Costs Absorbed by Others					19,063		19,063
Other - Current Year							
Liquidating Equity Activity (+/-)					(6,878)		(6,878)
Total Financing Sources	**$207**	**$0**	**$0**	**$0**	**$1,851,923**	**$(107,159)**	**$1,744,764**

Additional Accompanying Information
Consolidating Statement of Changes in Net Position
for the period ended September 30, 2003

(DOLLARS IN THOUSANDS)

	BATF		Eliminations		TOTAL		
	Cumulative Results of Operations	Unexpended Appropriations	Cumulative Results of Operations	Unexpended Appropriations	Cumulative Results of Operations	Unexpended Appropriations	Total
Less: Net Cost of Operations	$46				$3,171,681		$3,171,681
Net Position - End of Period	$440	$0	$0	$0	$(4,017,722)	$847,474	$(3,170,248)

On the Consolidated Statement of Net Costs, the costs are reported by major program using the SBA's cost accounting study, while on this statement the costs are reported by fund and are not allocated using the cost accounting study.